

UNITED STATES
COURT OF APPEALS
FOR THE NINTH CIRCUIT

. VAUGHAN,
Petitioner,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 17838

. VAUGHAN,
Petitioner,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 17839

REPLY BRIEF OF PETITIONER

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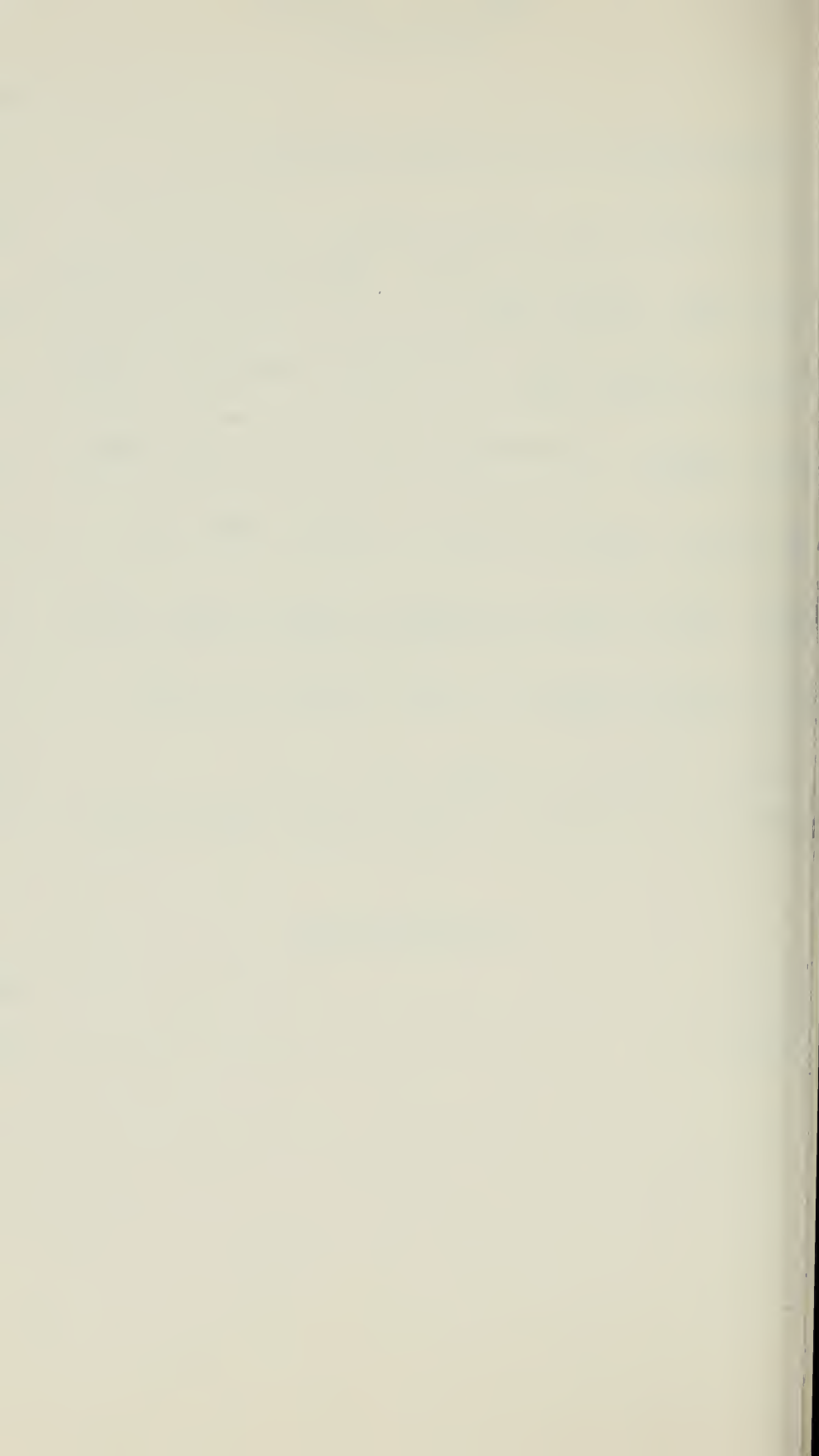
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UNITED STATES
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P. W. VAUGHAN,
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REPLY BRIEF OF PETITIONER



ARGUMENT

HEIFER CALVES DO NOT HAVE TO BE USED FOR BREEDING BEFORE THEY CAN BE CONSIDERED MEMBERS OF A BREEDING HERD FOR THE PURPOSE OF DETERMINING A TAXPAYER'S RIGHT TO CAPITAL GAINS ON THE PROCEEDS FROM THE SALE OF SUCH ANIMALS.

In the final analysis, the Tax Court's findings, and respondent's arguments in support thereof, are based on the premise that a heifer cannot become a member of the breeding herd until it has produced a calf. The court found this did not normally occur until the age of 24 months.

The law is clear that whether or not an animal is a member of the breeding herd is a question of fact which can only be established by evidence of the intent of the owner. The theory that an animal cannot be considered as a member of the breeding herd, and its sale result in long term capital gain, until it has reproduced has been specifically rejected by Congress and the courts. As was stated in McDonald v. Commissioner of Internal Revenue, (1954)(CA-2) 214 F.2d 341:

"Prior to this 1951 amendment the Commissioner had first refused to recognize that livestock could qualify for treatment under the capital gains provision, and then had ruled that only unusual reductions of herd would suffice. A series of adverse rulings in the courts, Albright v. United States, 8 Cir., 173 F.2d 339; United States v. Bennett, 5 Cir., 186 F.2d 407; Miller v. United States, D. C. Neb., 98 F.Supp. 948, led him to modify his position so as to allow such treatment of animals sold after being employed for substantially their full period of usefulness. Treas. Dept. Bull. June 17, 1951, Mim. 6660, 1951-2 Cum. Bull. 60. But all of the foregoing cases had given the section a far more liberal interpretation than this, granting favored treatment to the proceeds from young animals, and



in two of the cases from heifers (females which had never dropped a calf).

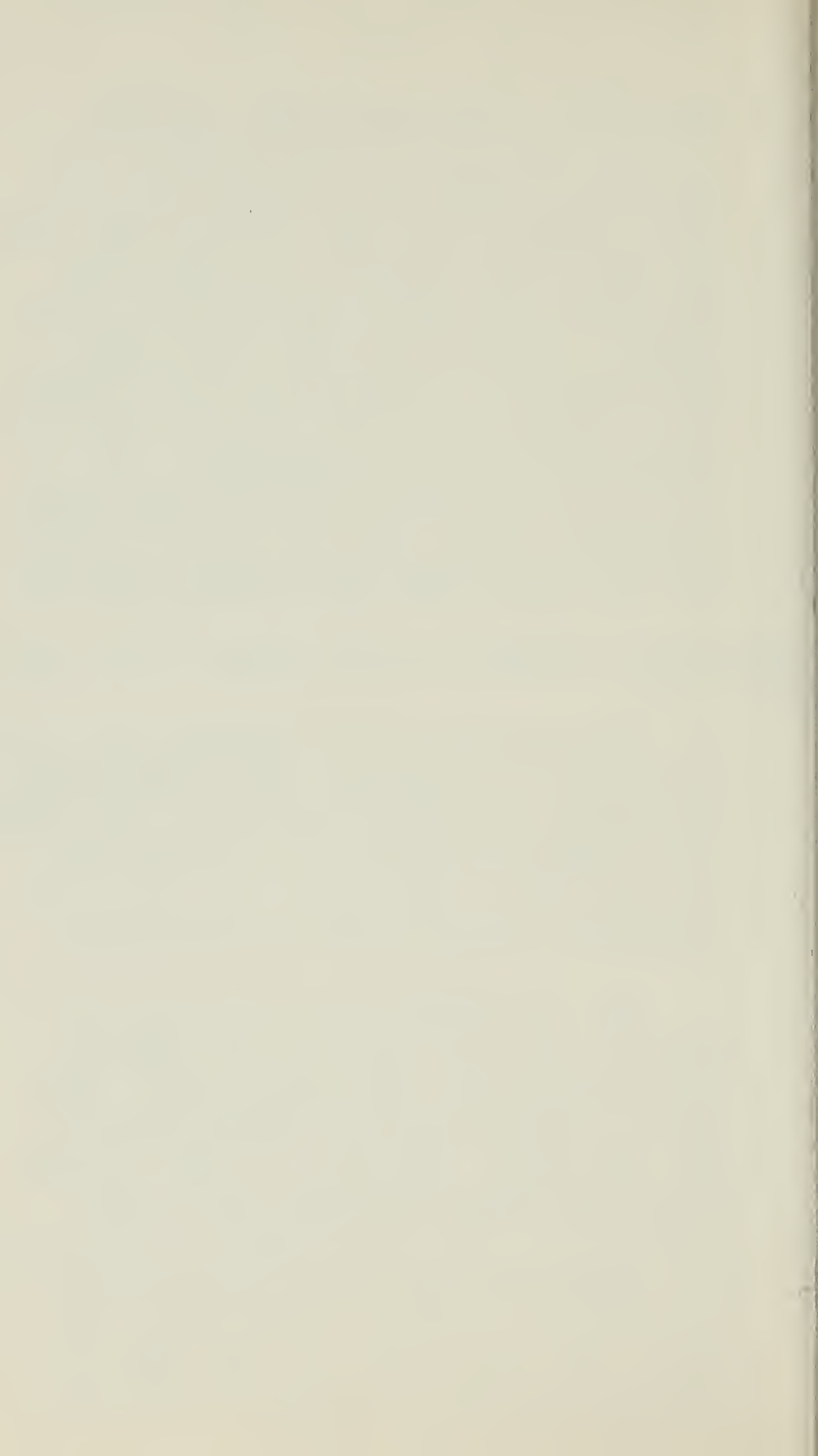
"When Congress undertook to amend §117(j)(1), it was made fully cognizant of this situation by representatives of livestock and breeding associations. Hearings before Committee on Finance on H.R. 4473, Revenue Act of 1951, Part. 3, pp. 1538, 1837, 2396; Sen. Rep. No. 781, 82d Cong., 1st Sess. 41-42. And it is manifest that the section was drafted with an eye to the breeders' complaints. Thus in defining property 'used' in the business the amendment speaks of livestock 'held' for an appropriate purpose, and adds the further proviso that it apply 'regardless of age.' The intent to repudiate the Commissioner's view is obvious, even without the specific statements in the Report of the Senate Committee on Finance, supra. And it is equally clear that the animal need not be mature and need not have been put to its intended use."

Similarly, in Estate of C. A. Smith, 23 T.C. 690, 707, the Tx Court stated:

". . .It is obvious that a breeding herd must be constantly replenished with young animals to continue its vitality. In the period when the younger animals are developing, presumably their immaturity alone is not conclusively determinative of the purpose for which they are being held. That is the fault with the respondent's proposed test; it would make immaturity conclusive.

"The legislative history of the 1951 amendment plainly indicates that Congress was concerned over the Commissioner's reluctance to recognize that young animals were capable of being held as breeding stock.⁶ And, the phrase 'regardless of age' written into the statute indicates a clear intent to prevent age alone from being used as the criterion. As the Fourth Circuit said, in commenting on the 1951 amendment in the course of affirming our decision in the Fox case, 'The important thing is not the age of the animals but the purpose for which they are held.' 198 F.2d at 722; cf. also McDonald v. Commissioner, (C.A. 2, 1954) 214 F.2d 341, reversing 17 T.C. 210 (1951)."

⁶ S. Rep. No. 781, 82d Cong., 1st Sess., pp. 41, 42



All testimony adduced at trial was to the effect that Vaughan and Milford intended that all heifers become members of the breeding herd at birth, in order to increase the herd to the capacity of the operation. The provisions of the agreement with Milford were consistent with this intent, wherein they provided an incentive to Milford to increase the breeding herd so that he would receive one-half of the increase at the termination of the contract. It is undisputed that Milford intended to increase the breeding herd to the maximum capacity of 2150 head of cattle, in order that he would have a herd of his own, from the increase, with which to stock his ranch at the termination of the contract.

Floyd testified as follows in answer to two questions:

"Q. (By Mr. Bailey) In so far as maintaining this herd of cattle turned over to Mr. Vaughan, what were the desires or purposes of the Vaughan Brothers partnership, what did you expect to accomplish so far as the size of the herd was concerned?

A. We expected and hoped to and wanted to build that herd of cattle right back up to where they had been in the prior years, back in the year '45. We felt there was ample room to do so and it was our hope and desire that that would be done.

Q. Now, when you say build it up to in 1945, you mean to a size of herd prior to the 1945 transaction to which you testified?

A. That is correct." (R. 160)

The testimony of Floyd on cross-examination and testimony of Milford and F. C. Vaughan to the same effect are contained in Appendix A, infra.

The respondent attempted to justify the court's finding that the heifers did not become members of the breeding herd until they reached the age of 24 months upon the basis that there was insufficient evidence to ascertain the reason for which such animals were held. To the contrary, all of the evidence produced at the trial was to the effect that the Vaughans and Milford intended that all heifers become members of the breeding herd at birth. An extract of the testimony of the Vaughans and Milford on this point is set forth in Appendix A.

It is interesting to note that the respondent in his brief in attempting to find support in the record for the court's finding had to go beyond the evidentiary record into the court's findings as indicated by his statement on page 20 of his brief:

"Milford testified (R. 344) that a heifer usually commences breeding at about 14 or 15 months. Since the gestation period lasts nine months (R. 438), most heifers did not produce a calf until they were approximately two years old. He also stated (R. 345-346) that a heifer can be considered a useful member of the herd at that age. In addition, the Tax Court found (R. 429) that 'The characteristics upon which a determination is made as to whether a heifer will be valuable as a replacement in the herd do not develop until the heifers are 18 to 24 months old.' F. C. Vaughan stated (R. 412) clearly that the culling of heifers was not satisfactory until they were 15 to 23 months old."

Respondent cites the record for most of his argument until he gets to the very meat of the nut where he suddenly switches, on page 20 of his brief, to the findings of the Tax Court for the following observation:

"In addition, the Tax Court found (R. 439) that 'The characteristics upon which a determination is made as to whether a heifer

will be valuable as a replacement in the herd do not develop until the heifers are 18 to 24 months old.'"

The evidence of the Vaughans and Milford on the question of intent is undisputed in the record and provides no support for the court's findings.

The intention of Milford and Vaughan was to retain every heifer in order to increase the breeding herd. However, even under these conditions it was necessary to cull out certain undesirable heifers. The actual testimony of Floyd, Milford and F. C. with respect to the culling and the selection of heifers for sale to provide Milford with operating expense money does not contain one word nor convey one inference that heifers were not selected for the breeding herd until they were 24 months old.

With respect to selection of heifers for sale, Floyd testified:

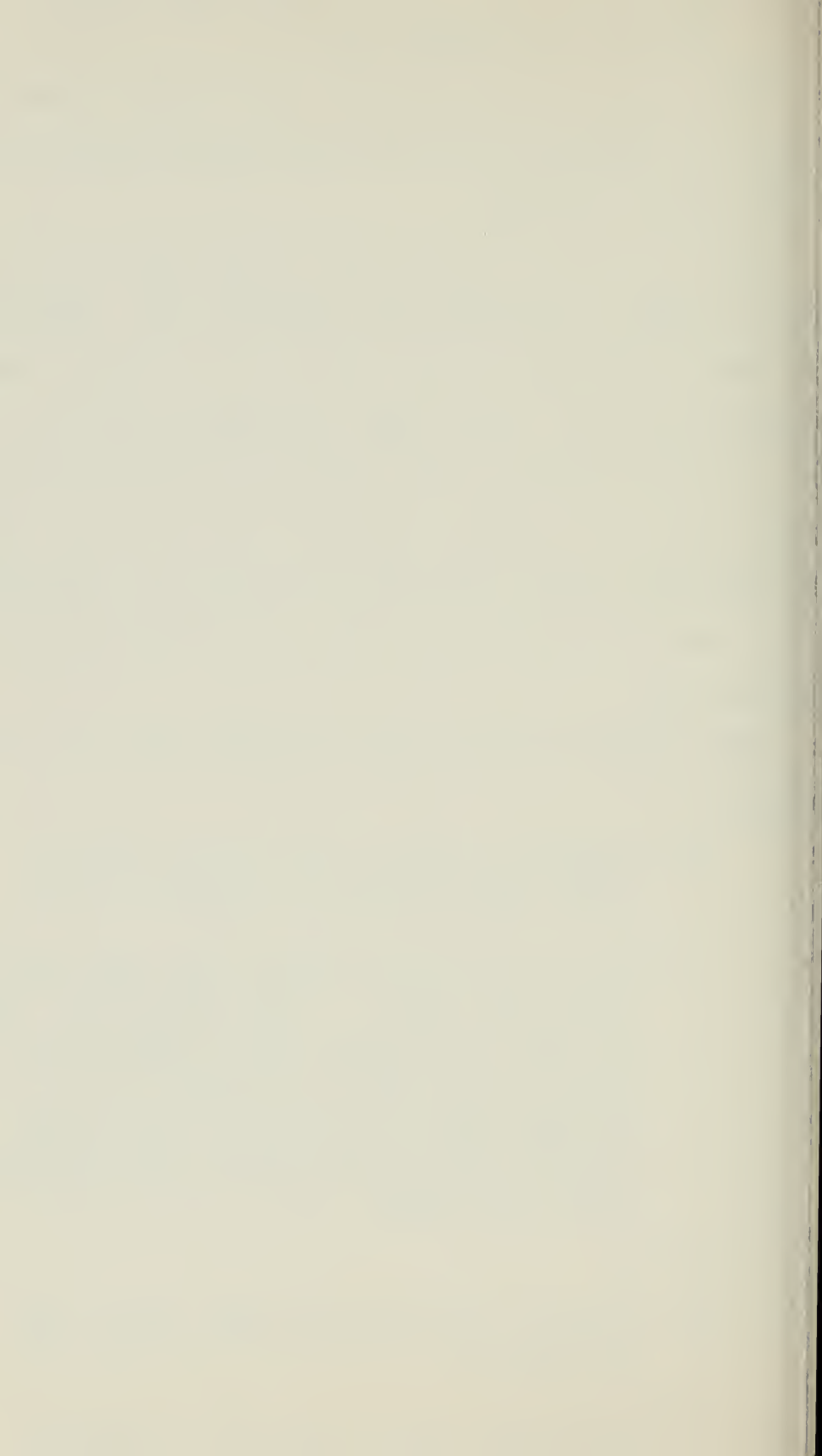
"Q. Whenever heifers are sold out of the range herd, how is the selection made as to what heifers to sell?

A. The selection of heifers that are sold out of an outfit is based on two or three different things. A man would sell, if he had two heifers, one of equal quality, one he could definitely tell she was going to produce an offspring, he would be much more-or less apt to sell that animal than one he couldn't tell whether she was going to produce an offspring or not." (R. 144)

* * *

"Q. How was the selection made out of the heifers to be sold out of a range herd of cattle?

A. I believe I did finish it, Mr. Bailey. That would be one basis of selection,



whether the animal was going to produce an offspring or whether she wasn't going to produce an offspring. Probably the next basis of selection would be her quality, her confirmation, her color, her build, that would probably be the next consideration.

Q. Is that all?

A. I believe so."

Milford's testimony was substantially the same. He stated the herd involved were range cattle, run on an open range, as differentiated from a purebred herd, or one operated in a fenced area. With respect to the selection of heifers for sale, the pertinent portions of Milford's and F. C. Vaughan's testimony are shown in Appendix B, *infra*.

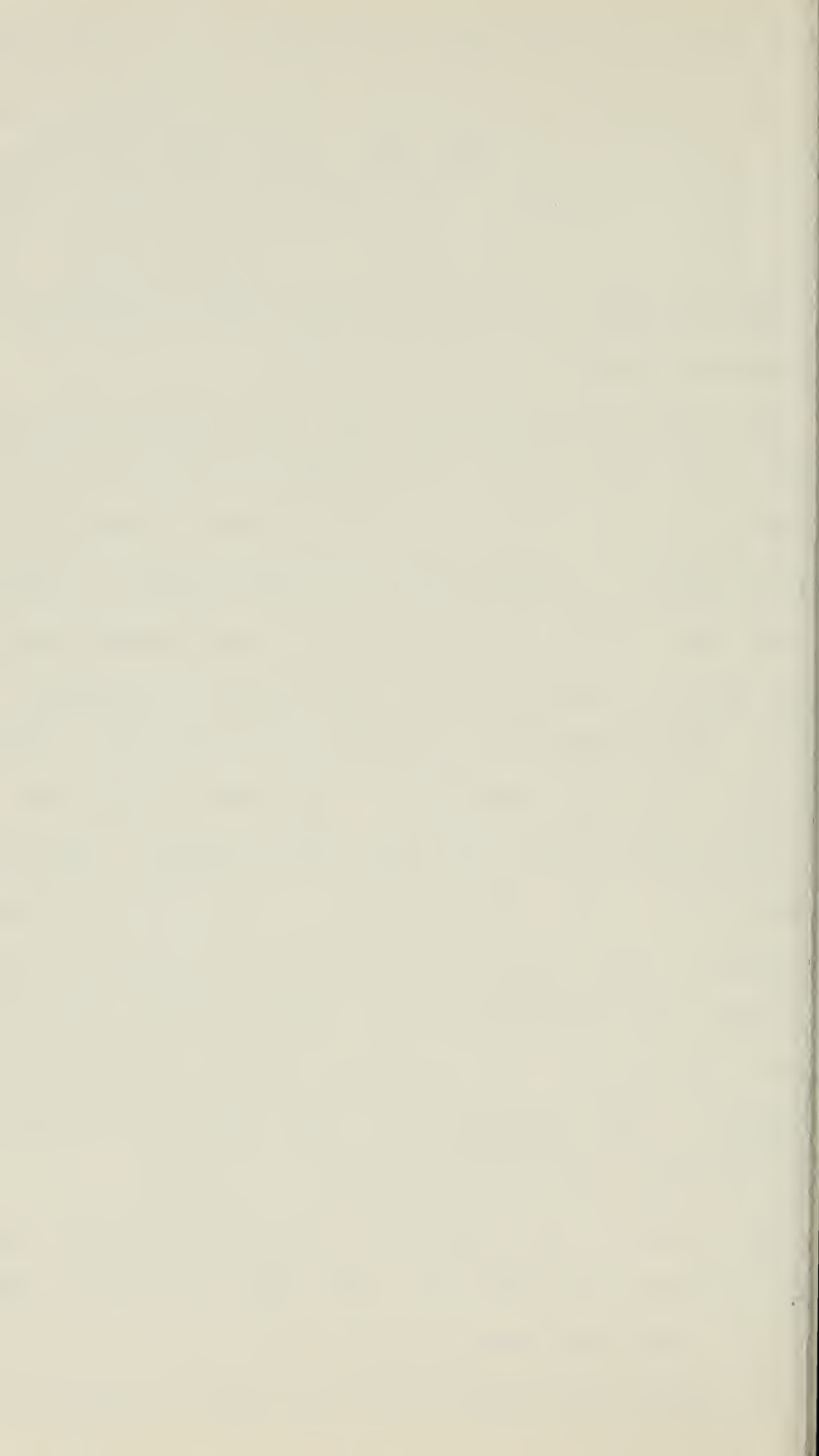
It is true that there were certain sub-standard heifers that would have been and were sold each year whether or not visibly pregnant. When it became apparent each year that heifers, other than the aforementioned culls, would have to be sold, visibly pregnant heifers were retained because they were obviously going to produce a calf and, secondly, because the cattle buyers didn't want to buy them. Finally, the remainder of the heifers sold were the less desirable ones, even though many good heifers were sold in order to provide funds so that Milford could pay off his bank financing.

The testimony shows that the best time to cull out the undesirable heifers because of long necks, long faces, bad coloring or poor confirmation is between the ages of 15 to 24 months. Both Milford and F. C. Vaughan testified that the culls were eliminated and sold at that age. However, those facts do not

support a finding that the heifers were not selected for the breeding herd until the age of 24 months. It is beyond cavil that Vaughan knew they would have to sell certain culls. However, the law is well settled that gain on the sale of culls, that were intended as members of the breeding herd until undesirable characteristics developed, results in capital gains. Similarly, those heifers sold out of the breeding herd because of unusual circumstances results in capital gains.

The evidence establishes that the steers were gathered for sale, and that certain cull heifers and cull cows were selected for sale, before any of the other animals were selected for that purpose. Through this culling process of heifers and cows, and the purchase and use of only registered thoroughbred Herford bulls, the quality of the herd was constantly being improved. When additional heifers had to be sold, they had to be selected from the remainder of the herd. Since the herd was not a scrub herd, those sold were good animals. Good husbandry, and selectivity, were ever present in the minds of both Milford and Vaughans, when heifers or cows were selected for sale. This selectivity was practiced for the obvious reason that the cattle retained constituted the remaining breeding herd to be returned to Vaughans at the termination of the contract, or to be divided between Vaughans and Milford as excess animals.

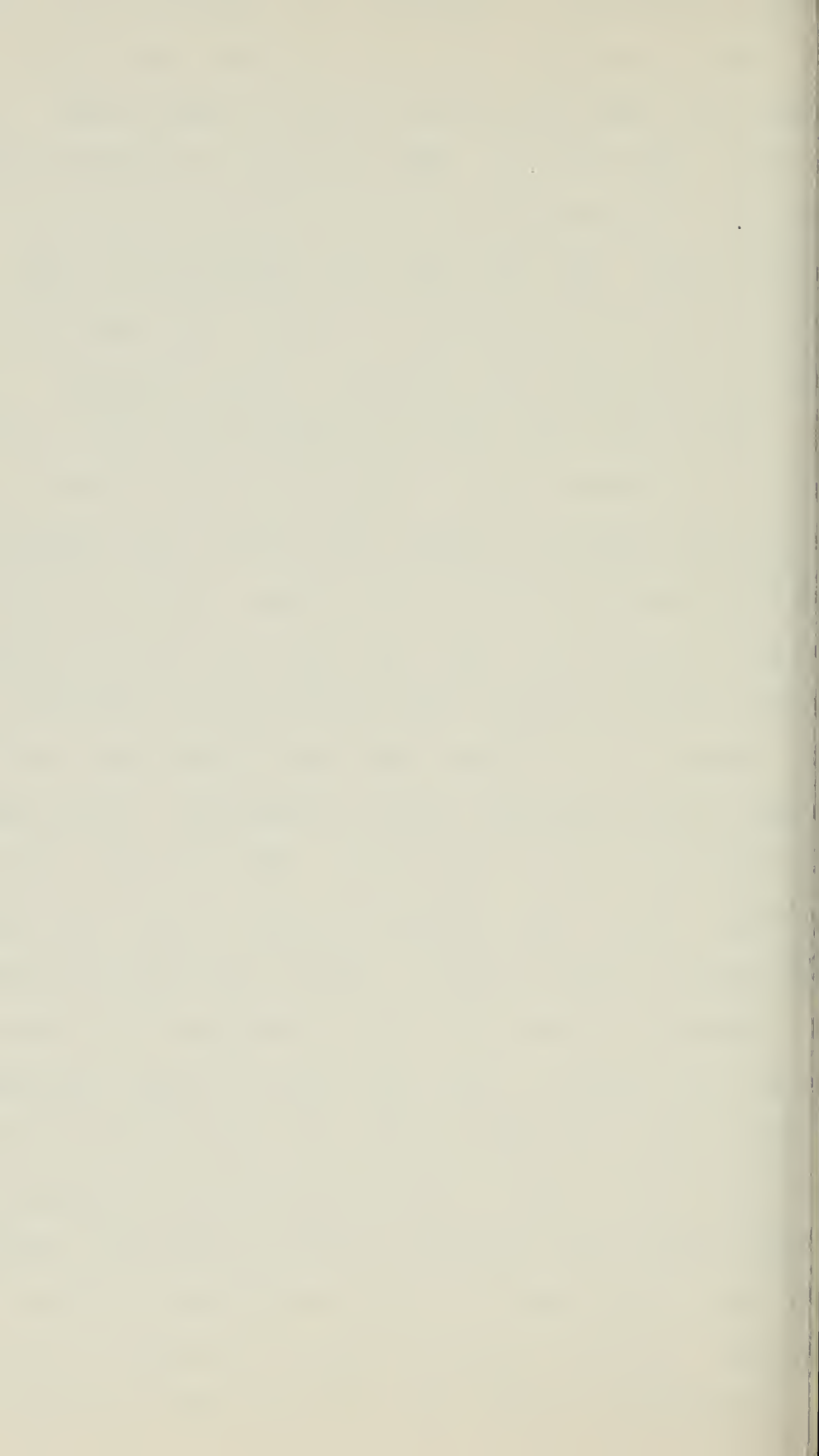
The cattle on this operation were operated as one herd. Neither Vaughans, nor Milford, ever had occasion to segregate any animals from the breeding herd. This was not an operation where the cattle were registered thoroughbred Herford, thus



making it necessary to segregate the breeding herd from the sale herd, and to segregate the bulls in order that birth records required for registered cattle could be maintained. This operation was a beef factory. They operated a breeding herd of range cattle for the production of beef steers for sale in the long yearling class. The only way the breeding herd could be increased was by the retention of heifers and exposure of them to bulls for breeding to the greatest extent possible. This they did. The heifers were never segregated for sale as "open" heifers. There is no evidence that a large proportion of the long yearling heifers were annually offered for sale or sold because of lack of operating facilities to care for them. To the contrary, the evidence is conclusive that the ranch was never stocked to its capacity of 2150 head of count cattle from 1946 until April 1, 1951. There is no evidence that the heifers were raised primarily for sale in the ordinary course of business. They were never advertised for sale to the public. This was not a herd of registered cattle that produced maximum income through the sale of the heifers and/or cows to others for breeding purposes.

Normally heifers will start breeding at 12 months of age. None of the heifers or cows that were sold had sucking calves at time of sale, and each animal was selected for sale because it did not have a calf or was not perceptibly pregnant. The sale of these animals was required, from an operating viewpoint, when there was a requirement for additional funds to keep Milford in operation. Milford could ill afford to winter a non-producer.

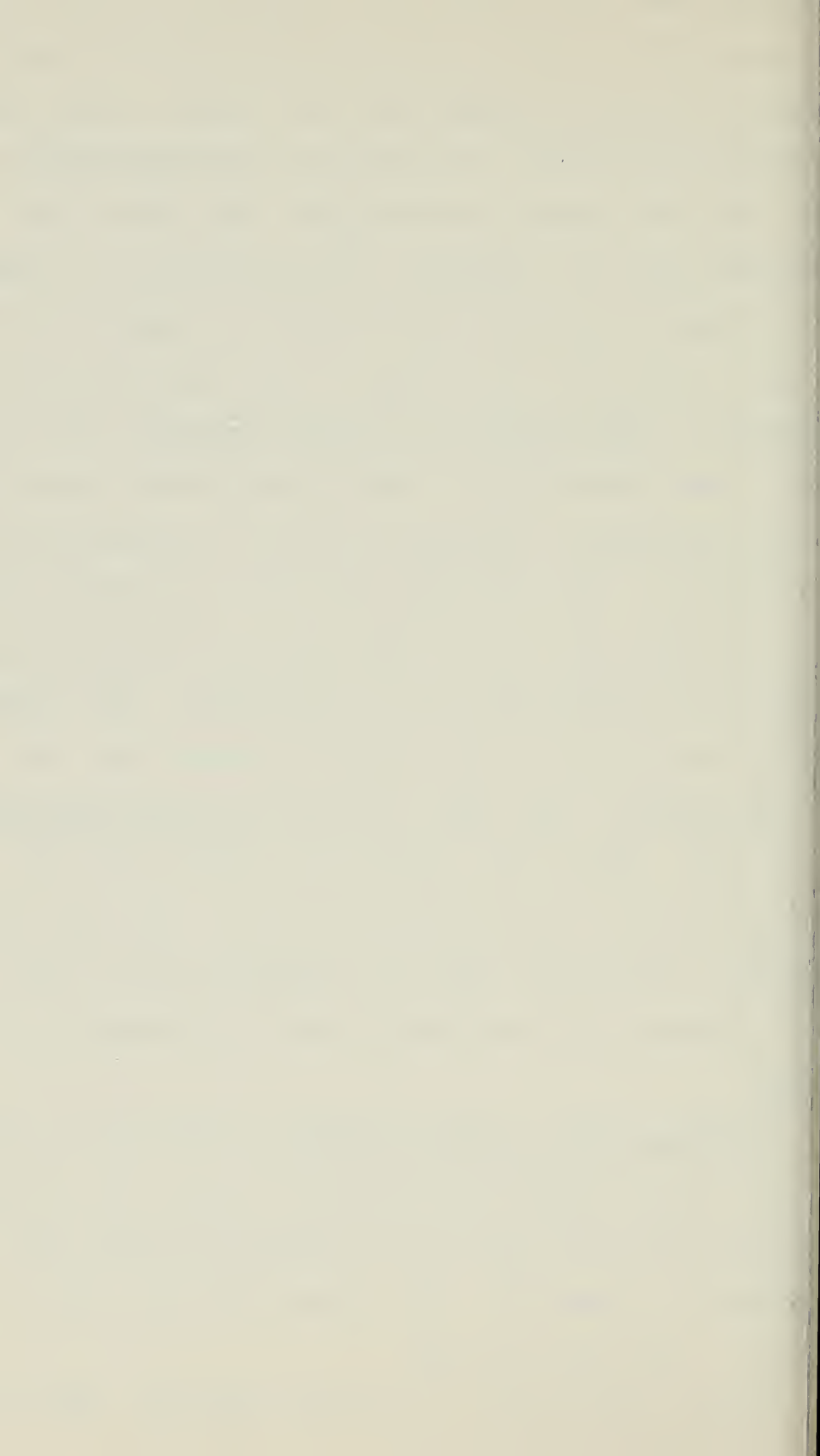
Respondent's brief cites several cases in support of his



contention that the heifers sold by petitioners were animals held primarily for sale in the ordinary course of business. Petitioners do not disagree with the results in the cases cited, but respectfully submit that they are distinguishable, on the facts, from the present proceedings. The cases cited dealt with registered herds of livestock. The operation of a registered herd of livestock permits the retention as members of the breeding herd of only the very finest of the heifers produced. In Gtfredson v. Commissioner of Internal Revenue, 217 F.2d 673, the animals were advertised for sale as registered animals and it was the petitioners' intention to sell a substantial portion of the offspring. The offspring could not be admitted as members of the breeding herd until they had proved themselves, heifers at age of 36 months and bulls at 48 months. The animals in question there were in each instance younger than the minimum age requirements. The same is true in William Wallace Greer, Jr., 7 T.C. 965. Many of the chinchilla rabbits sold had not actually been selected for the breeding herd since they had not proved themselves as breeders under the standards set by the petitioner before admission to the breeding herd of outstanding registered animals.

Biltmore & Co. v. United States, 228 F.2d 9, involved the sale of surplus animals that were not needed for either the herd or the reserve and could not be retained because the operation was stocked to capacity. The animals sold had never become members of the breeding herd.

Fox v. Commissioner of Internal Revenue, 198 F.2d 719, in-



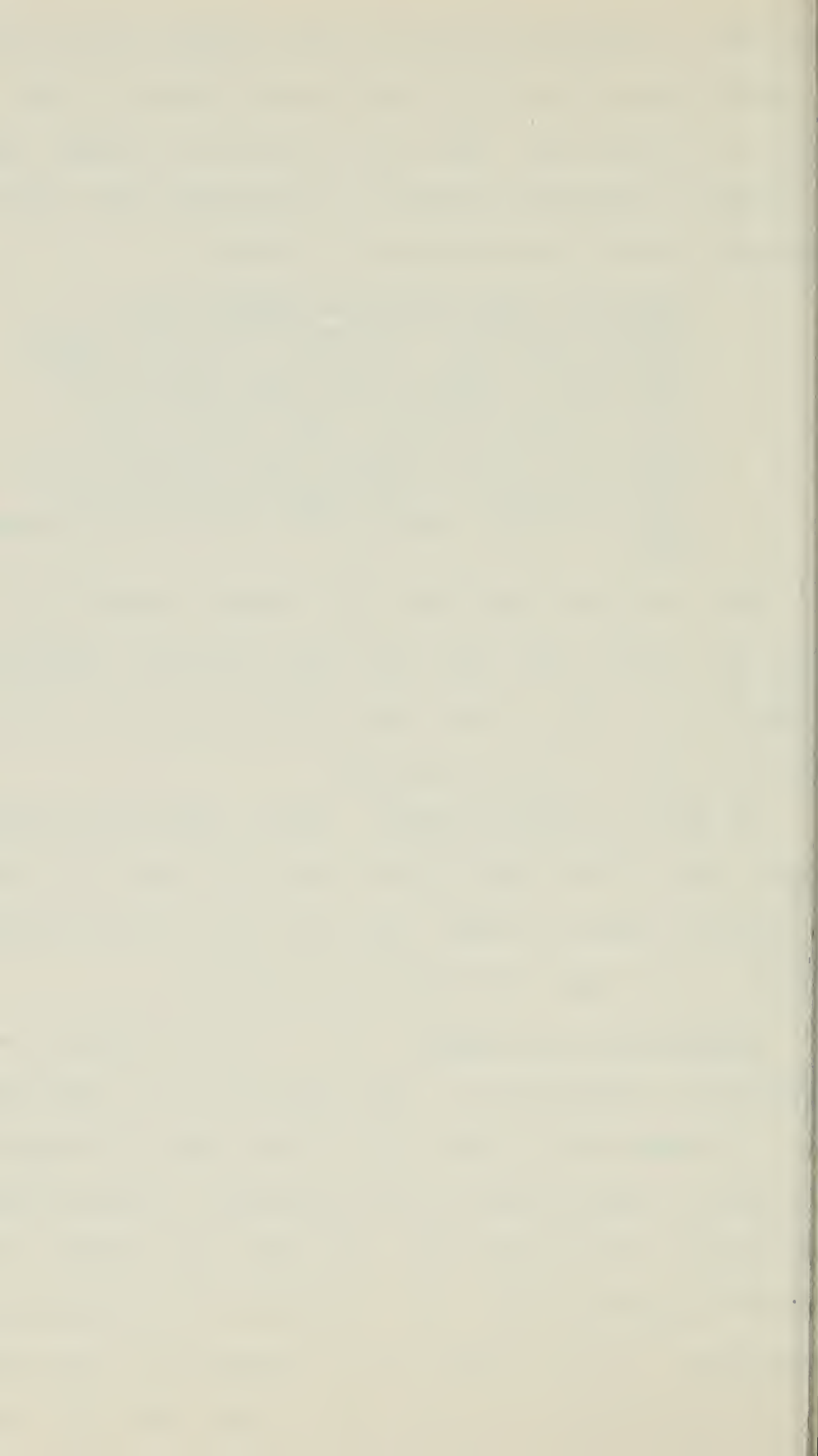
involved sales of thoroughbred, registered cattle. The court found there was no showing that any of the animals sold were part of the producing unit and that most were sold at an age before they could have become so. The court placed its finger squarely on the biggest difference between a registered herd operation and a range herd producing beef when it stated:

"Like all other persons engaged in a similar business (registered cattle herd) petitioners are, no doubt, alert to maintain and to improve the high quality of their producing unit; and to this end it may be that at times they select from among the calves raised some animals which they consider of such high quality as to justify their being placed in the producing unit . . ."

The evidence shows that the Vaughan operation raised all of their own heifers and cows and only purchased registered bulls to upgrade the herd. They were producing beef, not registered stock for sale to other breeders.

In Cole v. United States, 138 F. Supp. 186, the surplus animals sold from a high grade registered herd of cattle were not capital assets because there was never any intent on the part of Cole to use them for breeding purposes.

Estate of C. A. Smith, 23 T. C. 690, contains a very illuminating discussion of the operation of a registered purebred herd. A comparison of the facts with those in Vaughan points up that the two operations are as different as black and white. Smith very clearly illustrates that only the very finest offspring of a purebred registered herd are retained for breeding purposes. Furthermore, if the animals were intended for the breeding herd, the fact that they are sold before being bred will not prevent



m from being classified as held for breeding purposes. As

tofore noted, the court stated:

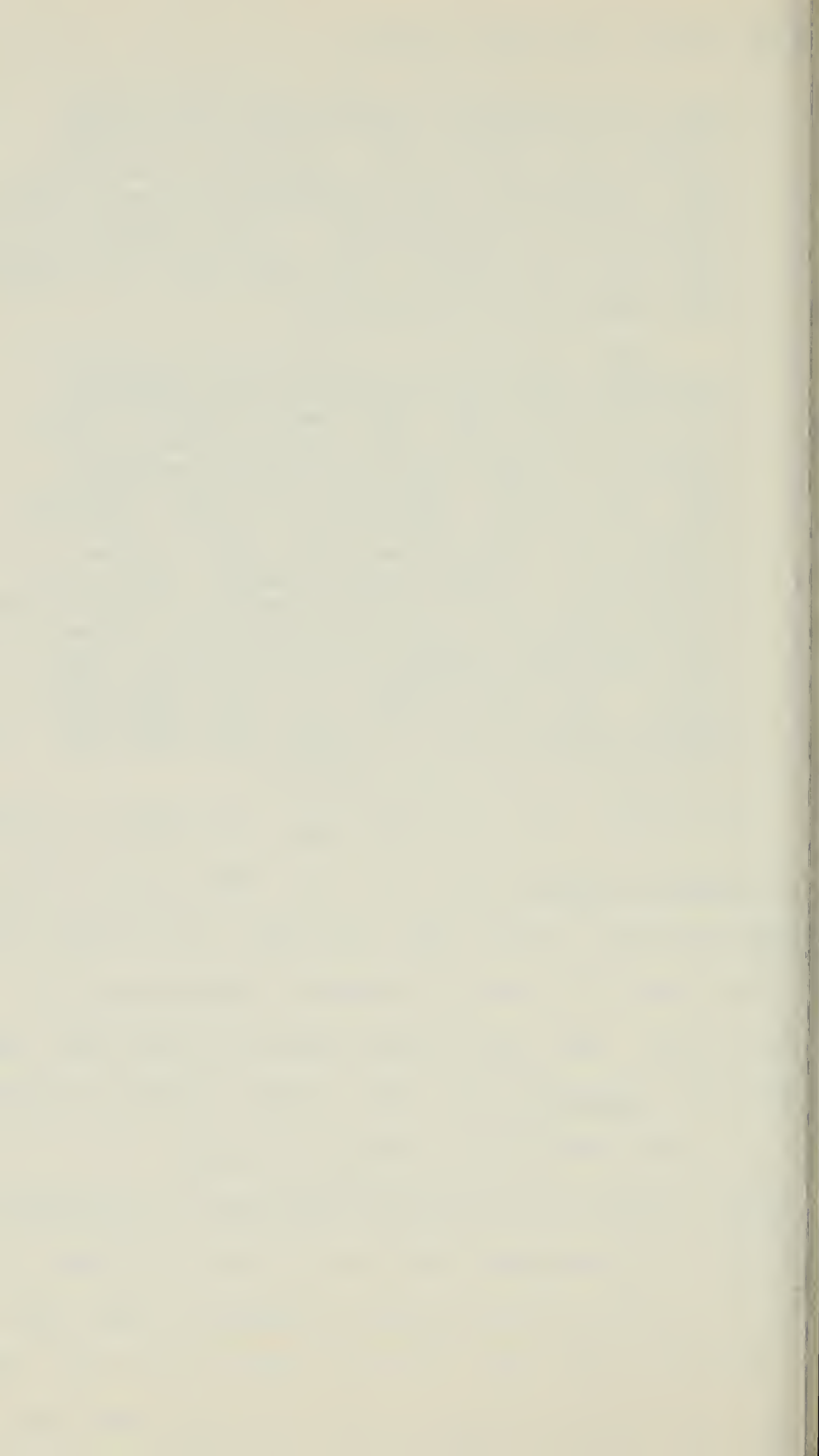
". . . It is obvious that a breeding herd must be constantly replenished with young animals to continue its vitality. In the period when the younger animals are developing, presumably their immaturity alone is not conclusively determinative of the purpose for which they are being held. That is the fault with the respondent's proposed test; it would make immaturity conclusive.

"The legislative history of the 1951 amendment plainly indicates that Congress was concerned over the Commissioner's reluctance to recognize that young animals were capable of being held as breeding stock.⁶ And, the phrase 'regardless of age' written into the statute indicates a clear intent to prevent age alone from being used as the criterion. As the Fourth Circuit said, in commenting on the 1951 amendment in the course of affirming our decision in the Fox case, 'The important thing is not the age of the animals but the purpose for which they are held.' 198 F.2d at 722; cf. also McDonald v. Commissioner, (C.A. 2, 1954) 214 F.2d 341, reversing 17 T.C. 210 (1951)."

⁶S. Rept. No. 781, 82d Cong., 1st Sess., pp.41-42.

In John L. Clark, (1957), 27 T.C. 1006, sales from a herd of registered breeding cattle were involved. The cattle were extensively advertised for sale as breeders and prospective buyers could take their pick. The court quite properly held that the cattle were held primarily for sale in the ordinary course of business and the proceeds resulted in ordinary income.

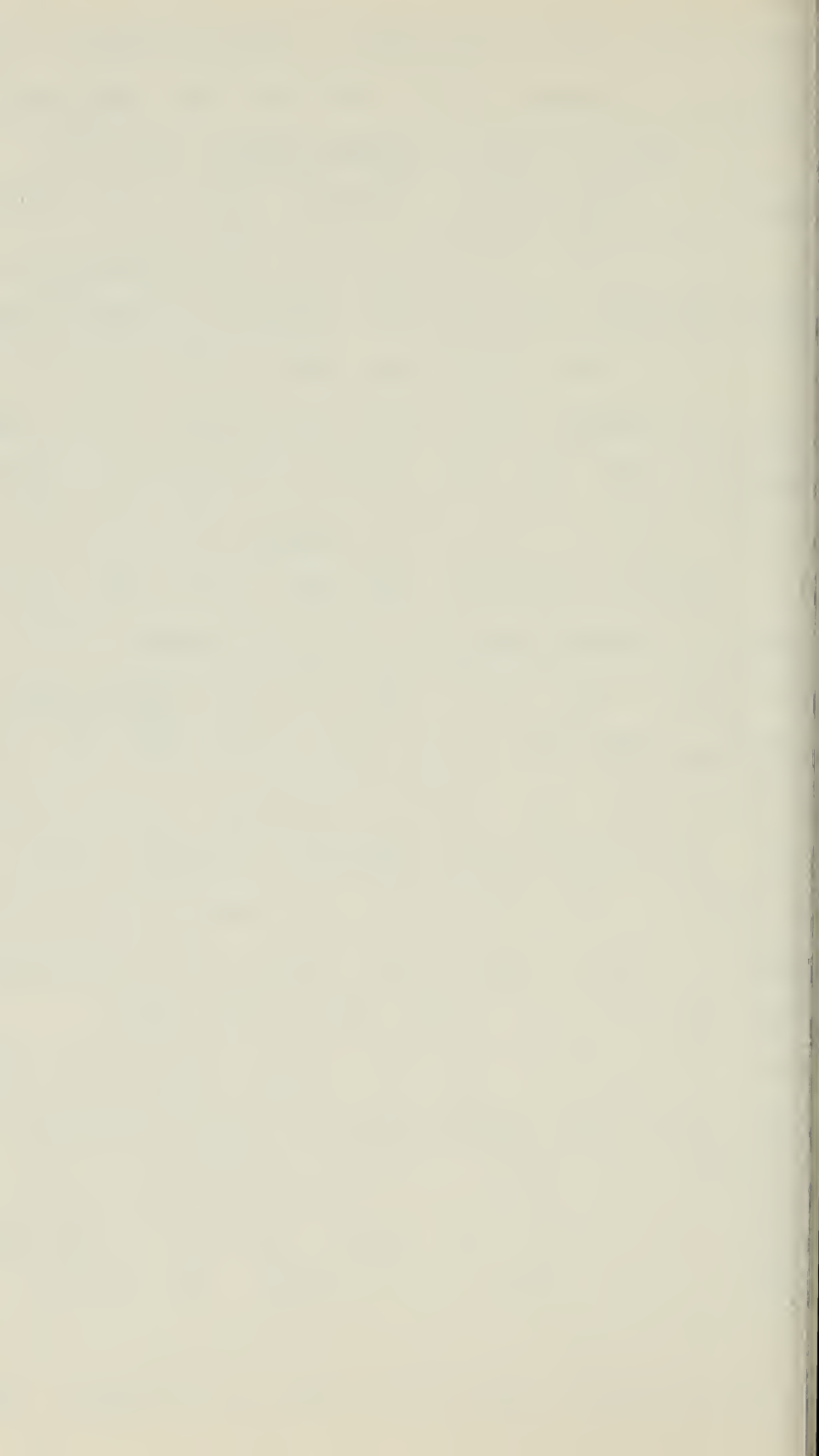
These situations involving admission of outstanding heifers into registered thoroughbred herds are a far cry from a typical range herd operation that primarily produces steer beef for sale. In an expanding range herd operation such as the one involved in the case, the heifers remain in the breeding herd unless culled



an age when undesirable characteristics appear.

Petitioners rely on Albright v. United States., 173 F.2d 339; United States v. Bennett, (CA-5) 186 F.2d 407; Fawn Lake Ranch Co., T.C. 1139; Miller et al v. United States, USDC Neb., 98 F.Supp. 4; Pfister v. United States, USDC So. Dak., 102 F. Supp. 640, and on another point, CA-8, 205 F.2d 538; McDonald v. Commissioner of Internal Revenue, 214 F.2d 341; O'Neill v. United States, USDC Dist. Calif., 52-2, USTC Para. 9462, aff'd CA-9, 211 F.2d 701; Estate of C. A. Smith, 23 T.C. 690, acq. 1956-1 CB 5; Deseret Live Stock Company, Para. 53, 093, (1953) P-H Memo T.C.; Bartlett, T.C. 55,259 (1955) P-H Memo T.C.; Smith, Para. 56,030 (1956) P-H Memo T.C.; Miller v. Connell, USDC West. Dist. Mo., 56-1 USTC, Para. 103; Carter v. Commissioner of Internal Revenue, CA-5, 257 F.2d 10, reversing in part 16 T.C. Memo 280; and Harder, et al v. United States, USDC East. Dist. Wash., 59-1 USTC Para. 9364. All these cases have been cited and discussed in petitioners' opening brief. Petitioners again emphasize, however, their contention that the facts in this proceeding fully establish petitioners' entitlement to capital gains from the sale of the heifers in question under the rationale of the above cited cases.

Even if we were to adopt the theory apparently relied upon by the Tax Court that a heifer must be actually used as a member of the breeding herd before it can be considered a part of said herd, the evidence would not support the court's finding that the heifer had to reach the age of 24 months. The evidence is clear that the heifers begin breeding at about the age of 12 months and at least 50% produce a calf by the age of 24 months. If the test



be applied is the actual use of the animals for breeding purposes, it is obvious that the animals were in fact used as a part of the breeding herd at the time they were bred which of necessity had to be 9 months prior to the time they produced a calf, which for some reason seems to be the magic date relied upon by the respondent. Thus, the animals were used for breeding at 12 months. Marshall Anderson, a cattle buyer who testified for petitioners, stated that even though he tried to purchase non-pregnant heifers, he usually 40% to 50% of the heifers purchased from a range herd were pregnant. From this it would follow that in any event at least 50% of the heifers sold by petitioners had actually been bred prior to sale. (R. 388-389)

Respondent insists that the test of whether or not an animal is a member of the breeding herd turns on whether it is a productive member of the herd. On page 15 of his brief he contends that the amendment to Section 117(j), Internal Revenue Code of 1939, by Section 324 of the Revenue Act of 1951, C. 521, 65 Stat. 452, was to preserve capital gain treatment even though an animal held for breeding purposes was sold before its breeding usefulness had ended. This misapprehension strikes at the very heart of this controversy and at the risk of being repetitious respectfully call attention to what was said in McDonald v. Commissioner of Internal Revenue, (1954) (CA-2), 214 F.2d 341, and the Estate of C. A. Smith, 23 T.C. 690, 707, as heretofore set forth at the beginning of this brief.

These interpretations expressed by the courts indicate that Congress was concerned about disallowance of capital gains on



ing animals in the breeding herds and not, in the words of the respondent, animals sold before their usefulness had ended.

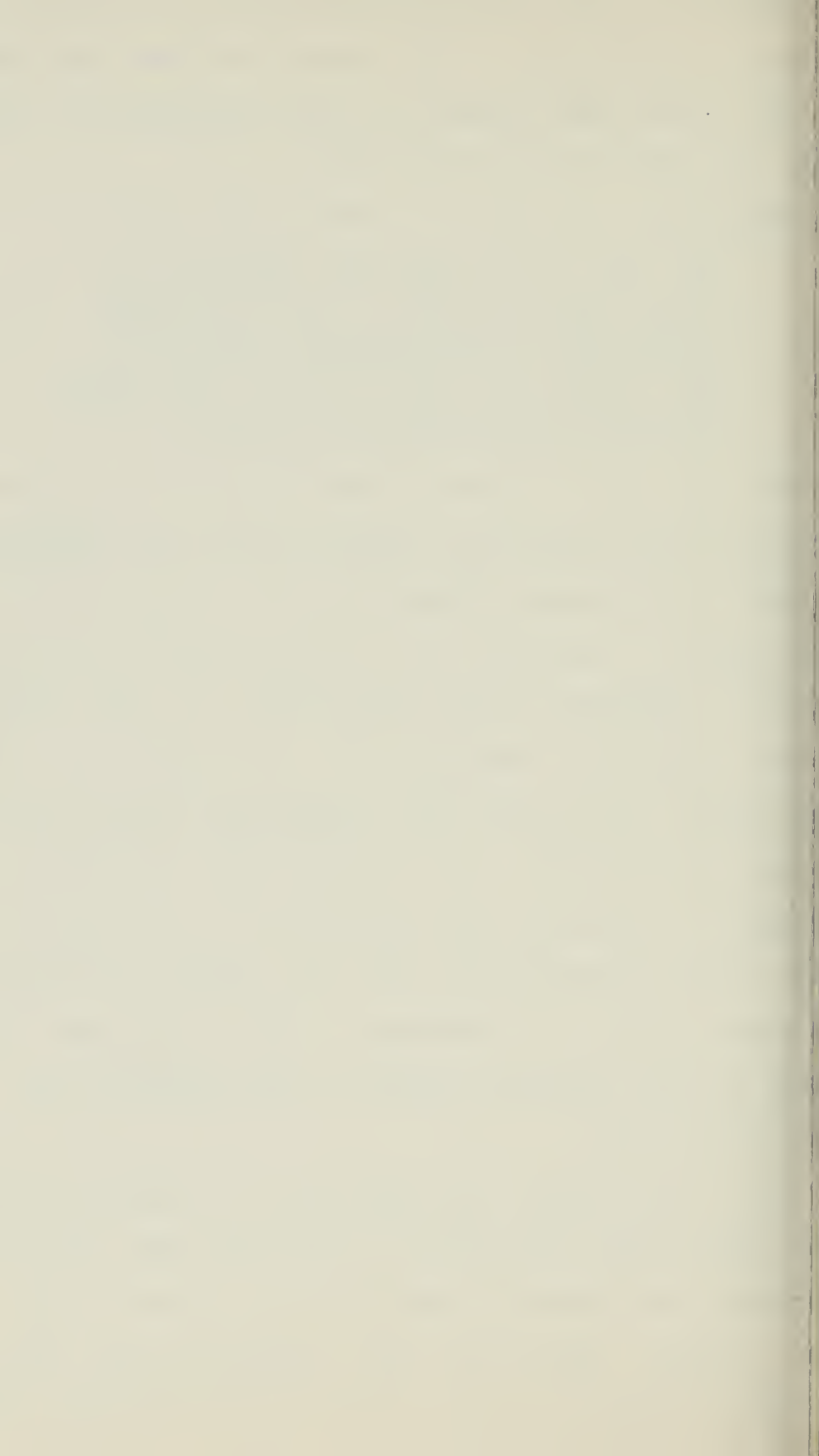
The actions and arguments of the respondent in this matter reflect his position of 20 years ago.

Respondent, on page 23 of his brief, states:

"The fact, upon which the taxpayers so strenuously rely, that they were forced to sell these animals is of no material consequence. The immediate reason for sale is not the crucial factor; the essential question is the reason for which the animals were held prior to sale."

The only facts recited by the Tax Court in support of its position that the animals in question were held primarily for sale, which are actually supported by the record, are the sales of the animals. Obviously, if the sales had not been made, we would not be engaged in this controversy. Is bare evidence of sales sufficient, standing alone, to justify the holding of the Tax Court? If it is, this taxpayer and others selling breeding stock can never prevail. It is petitioners' position that since the animals in question were intended to be, and were treated as members of the breeding herd, that the reason for the sale must be examined in order to determine if the act of sale is actually contrary to the expressed intent of the taxpayers that the animals were breeding stock.

Where the taxpayer was operating at capacity, obviously sales other than replacements, sold each year, were not intended for breeding stock despite expressions of intent of the taxpayer to the contrary. Similarly, where taxpayers breed registered and purebred stock for sale, sales from the breeding herd are

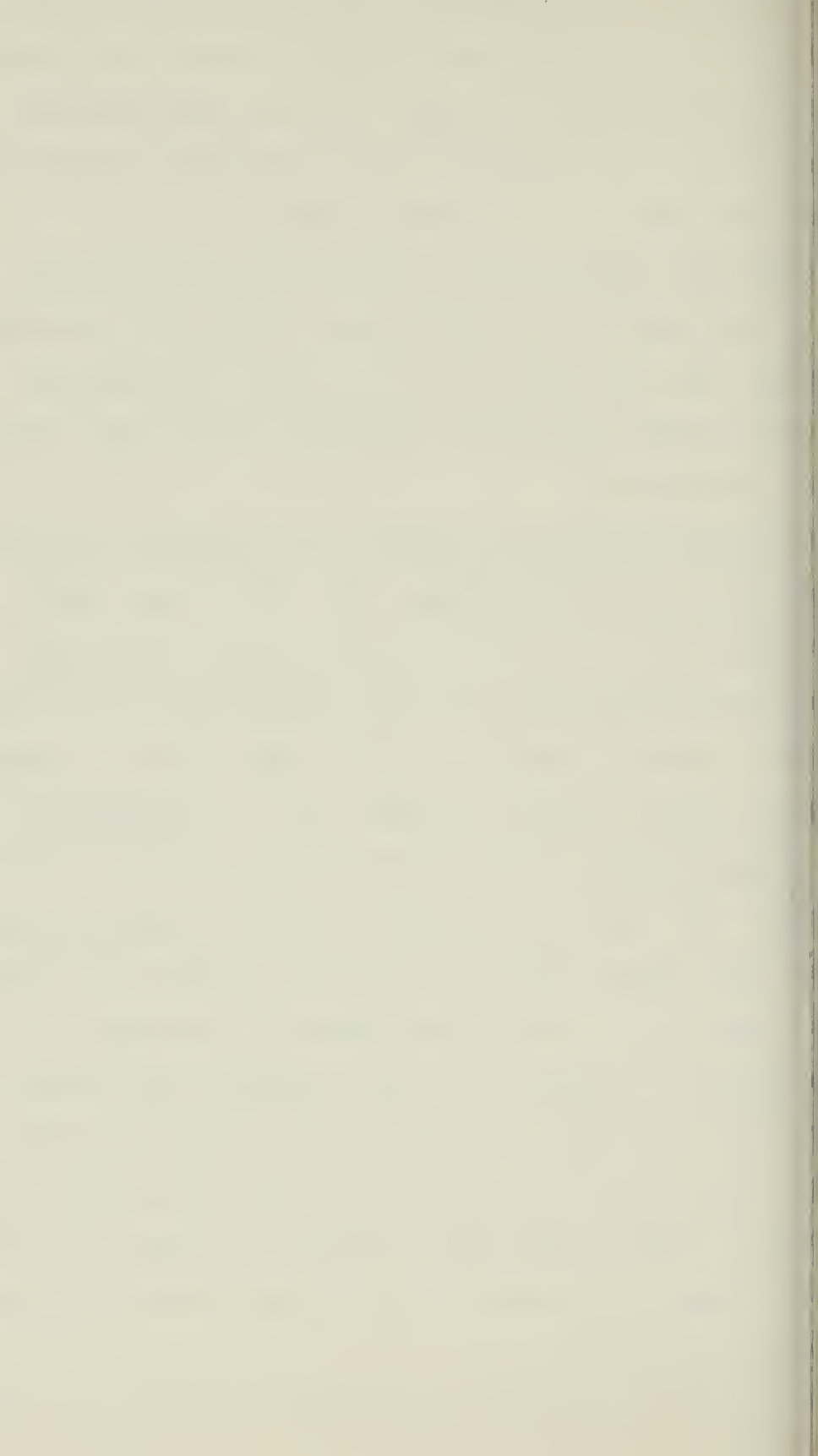


at contrary to the expressed intent that the animals were breeding stock. On the other hand the courts have held that sales of breeding heifers under certain conditions are not acts contrary to or inconsistent with the expressed intent that the animals were part of the breeding herd.

Even the Commissioner's Regulations 118, Section 39.117-1(b)(2), anticipate that even though animals are intended for breeding, they may have to be sold where circumstances change and such intended purpose is prevented by accident, disease, or other circumstances.

In United States v. O'Neill, (1954)(CA-9) 211 F.2d 701; Warner, et al v. United States, 59-1 USTC, Para. 9364, USDC East. Dist. Wash; sales of unbred heifers because of adverse range or breeding conditions were not sales inconsistent with intent that they were breeding animals. To the same effect in Deseret Live Stock Co., Para. 53,093, P-H Memo. T.C., and Carter v. Commissioner of Internal Revenue, (CA-5) 257 F.2d 595, rev'd in part 16 T.C. 10-280. The same decision was reached in Estate of C. A. Smith, 10-690, where taxpayer continued to show his breeding stock despite the fact he had to sell them if requested. In Bartlett, Para. 55,259, P-H Memo. T.C., the taxpayers sold immature heifers because of a shortage of funds and the court held that the sale was not inconsistent with the intent that the animals were breeding stock. These cases were discussed in detail in our opening brief on pages 11 through 22 and in the interest of brevity are all summarized here.

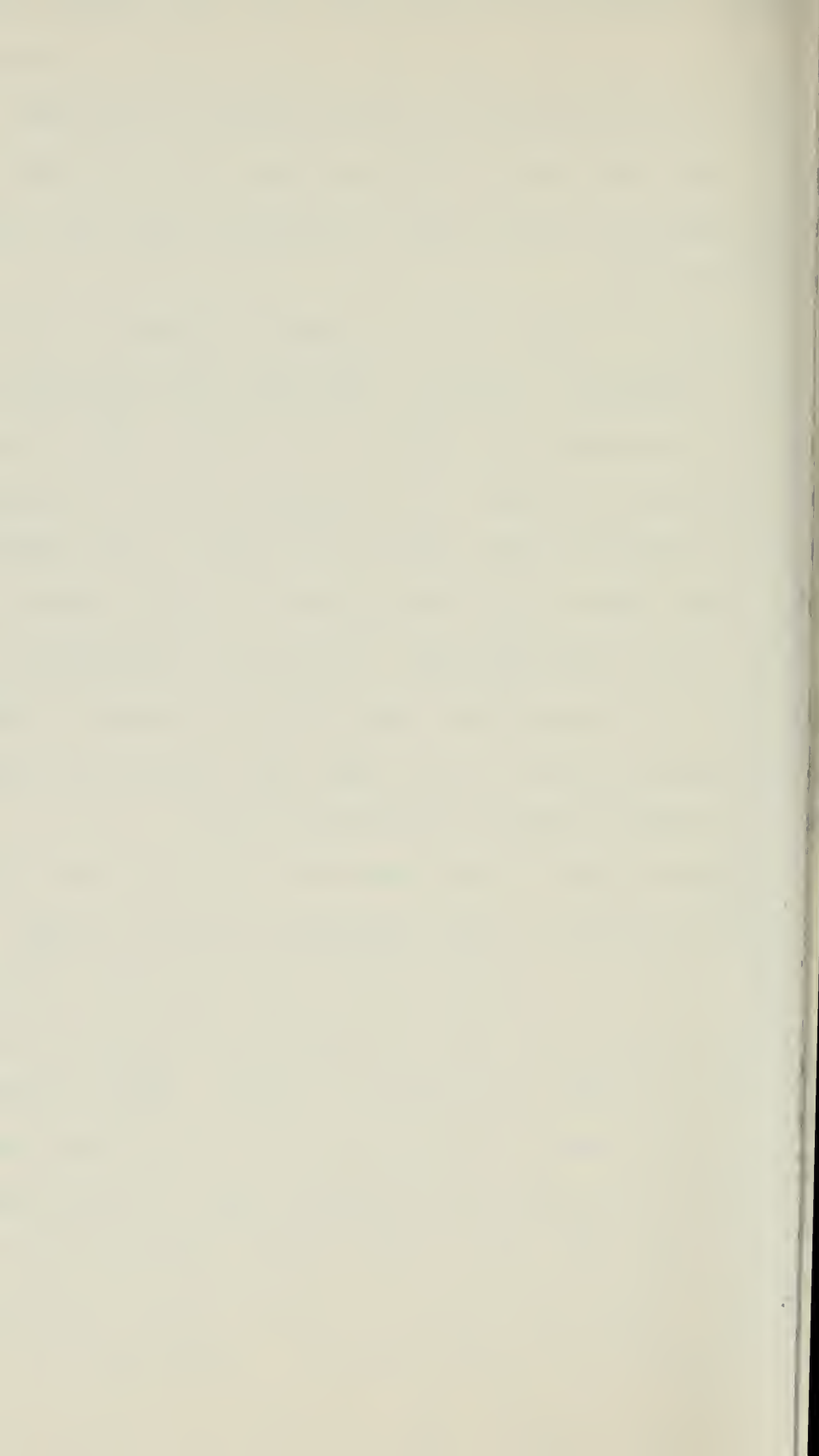
In view of the facts established in this case, it is



respectfully submitted to this Court that the reason for the sale of heifers is important, and that in view of the reason, that sales had to be generated to permit Milford to perform under the contract, that the sales, standing alone, are not acts inconsistent with the expressed intent that the heifers sold were members of the breeding herd.

On page 26 of his brief respondent states he is unable to comprehend taxpayers' argument regarding the applicability here of certain principles set forth in I.T. 3712, 1945 C.B. 176, since the I.T. had been revoked. The taxpayers do not contend that I.T. 3712 has not been revoked. We do say that it was issued at a time when the Commissioner would permit capital gains only on a disposition of the breeding herd. With each successive ruling on the subject the Commissioner was forced to accede to the various court decisions adverse to his stand and liberalize his views with respect to capital gains on breeding cattle.

Taxpayers point to the tests set forth in I.T. 3712 as being a reasonable approach by the respondent even at a time when his restricted views as to capital gains were far more restrictive than could be justified after amendment of Section 117(j), Internal Revenue Code of 1939, by Congress in 1951. Those tests in I.T. 3712 recognized some of the realities of a livestock operation. Namely, that if animals are raised for sale as beef they are sold when they fall when they are in their best condition and they are not carried through the winter on feed. Winter feeding is the greatest expense of a range operation. Certainly the sale of heifers in March or April, 1951 indicates that they were not



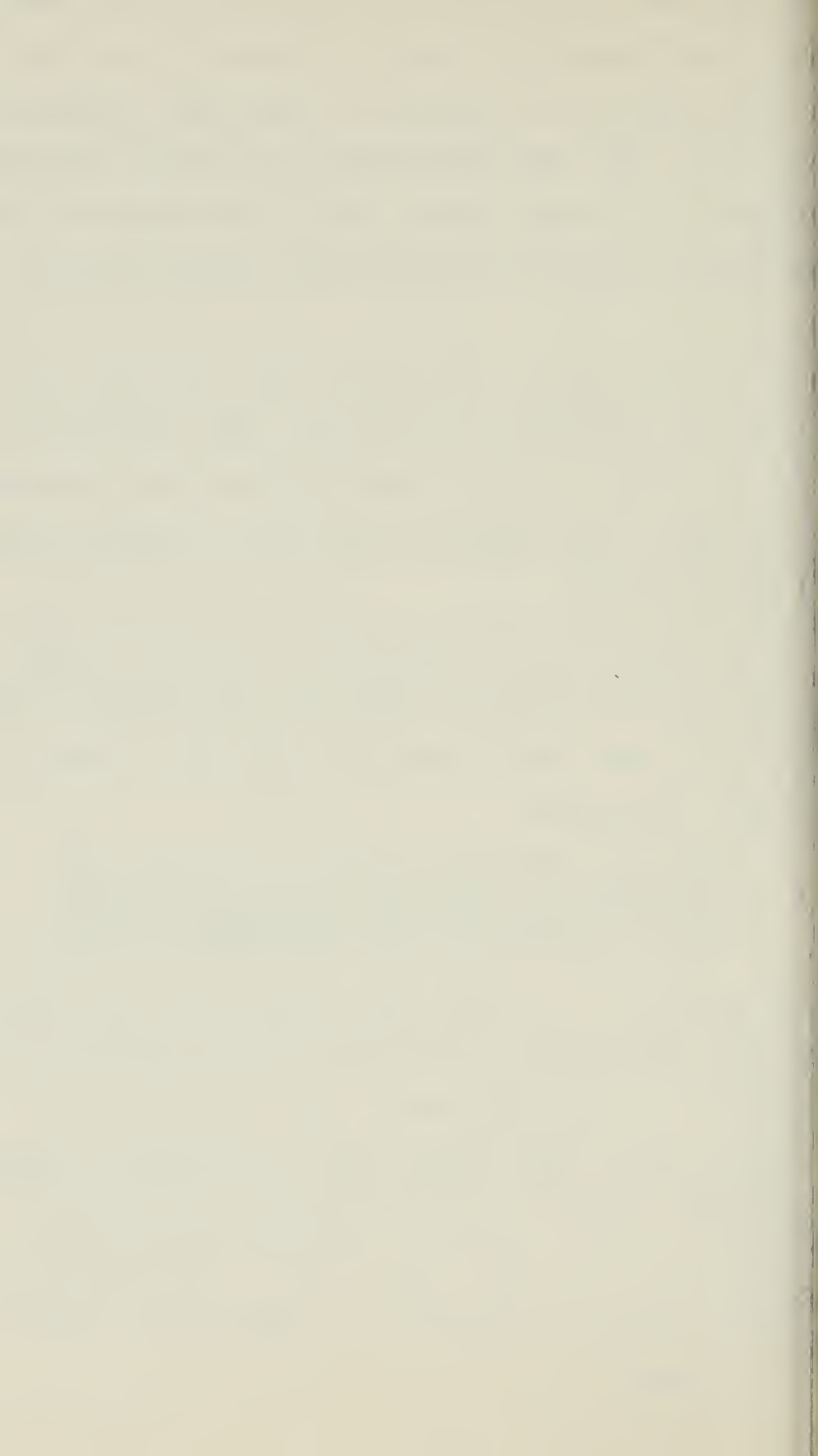
ntended for beef in 1950 and were only sold under emergency
onitions and represent a partial liquidation of the breeding
er. Here again is a situation, the partial liquidation of a
reeding herd, that the Commissioner of Internal Revenue early
ecognized as producing capital gains even before the Congress
ned Section 117(j) of the Internal Revenue Code of 1939 in
75.

It is petitioners' contention that the tests laid down in
T 3712 were reasonable then and the same tests are still
asonable in this situation where heifers from the breeding
r were sold in the spring of the year in partial liquidation
he breeding herd.

It is apparent from respondent's comment on page 26 of his
lf that he also does not comprehend the meaning of Section
in the Revenue Act of 1962, P.L. 87-834, 76 Stat. 960,
ion 13. He states:

"Section 1245 was designed to prevent the
conversion of ordinary income into capital
gain in situations where excessive deprec-
iation deductions were taken prior to sale."

An analysis of Section 1245 reveals that the prevention is
nst all depreciation after the effective date and "excessive
eciation" is not mentioned in that section at all. Clearly,
Revenue Act of 1962 changes the tax treatment respecting gains
epreciable personal property (except livestock) by making any
s on the sale or other disposition of such property taxable
rdinary income to the extent of depreciation deductions
iously taken.



Under the Tax Court's decision in this case they have abandoned their position in Estate of C. A. Smith, supra, where we state that a balanced breeding herd must contain heifers of all ages for purposes of continuity. Here there are absolutely no heifers under the age of 24 months considered by that court as members of the breeding herd. In 1951 Vaughan sold every heifer he owned under the age of two years, but despite this none were treated as members of the breeding herd.

CONCLUSION

In view of the foregoing, it is respectfully requested that the Court find that petitioners are entitled to report as capital gains under Section 117(j) of the Internal Revenue Code of 1939 the gain realized from the sale of the heifers for the years 1948, 1949, 1950 and 1951.

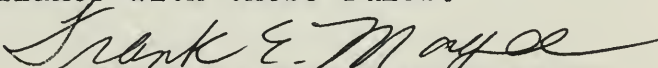
Respectfully submitted,

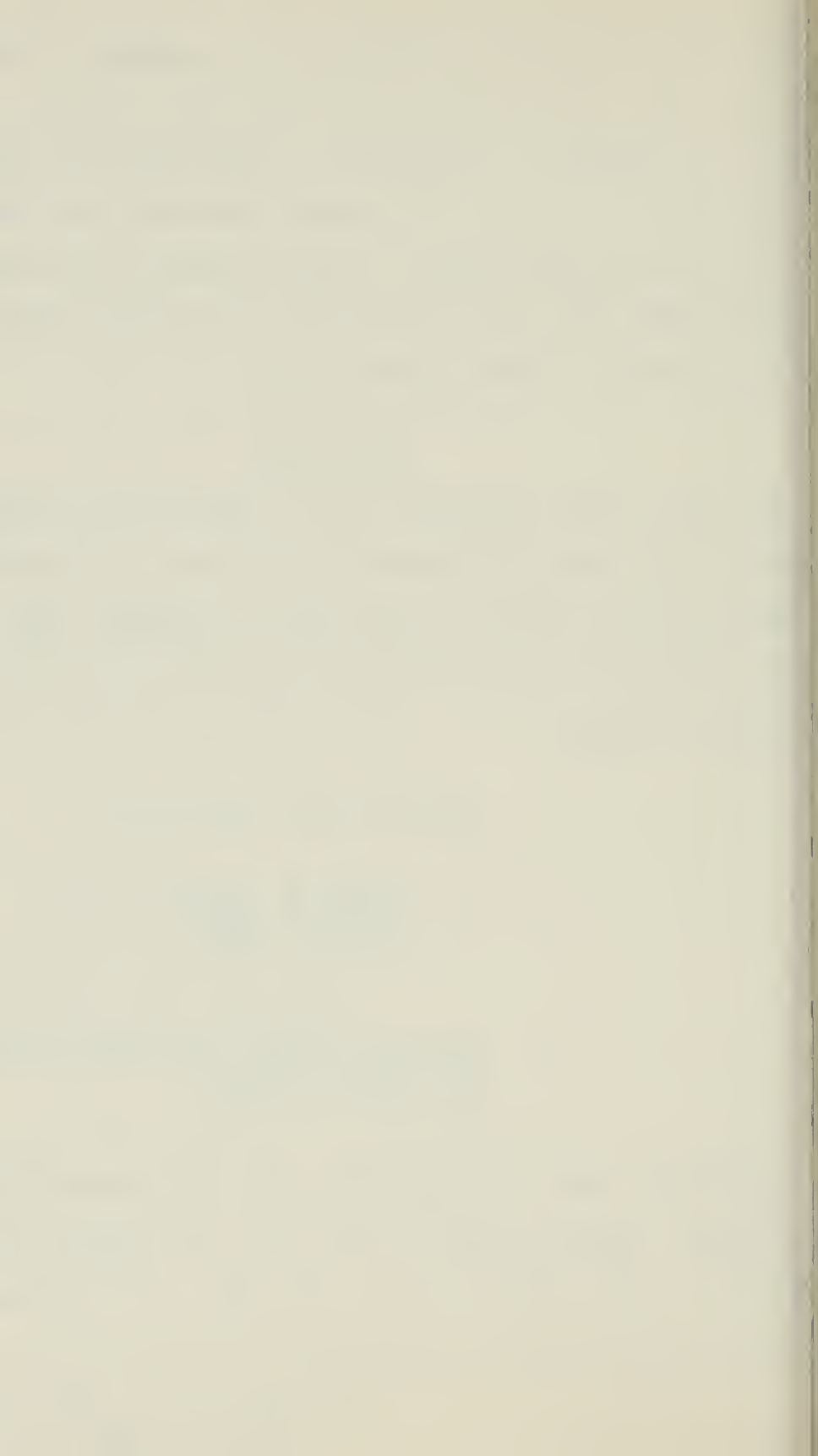
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I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion the foregoing brief is in full compliance with those rules.


Frank E. Magee, Attorney



APPENDIX "A"

mony of Vaughans and Milford Vaught regarding intent
which heifers were held.

On cross-examination Floyd testified:

"Q. (By Mr. Picco) You wouldn't want to sell any if you had the opportunity, is that right? I thought you said at the beginning you were trying to keep all the heifers in there?

A. We were.

Q. At least you were trying to get up to a certain point with that herd, that is correct?

A. That is correct.

Q. But you found every year you were selling forty to fifty per cent of the heifer crop every year?

A. I wouldn't agree with that statement.

Q. I am trying to follow you, tell me what you were selling every year in the way of heifers?

A. We were selling whatever heifers were necessary to sell.

Q. You found that every year it was necessary to sell forty to fifty per cent of the heifer crop?

A. Again in the '48, the ninety-four heifers wouldn't be fifty per cent of the heifer crop.

Q. What per cent would it be?

A. Possibly thirty to thirty-three per cent.

Q. Mr. Vaughan, I can understand how you couldn't possibly predict that the sale of heifers would be necessary in 1947, the first time it happened, but when you tell this Court that that happened every year throughout the lease agreement, do you expect us to believe that, that you didn't know at the beginning of each year you would have to sell a certain number of the heifers?

A. I don't think that anyone knew that a heifer would have to be sold and it was surely our desire not to sell any."

Milford testified on direct examination:

- "Q. And at the time you entered into this agreement, Mr. Vaught, what was your idea about the size of the herd, what plan, if any, did you have in mind about the size of the herd during the course of this operation?
- A. To build it just as big as I possibly could so at the termination of the lease I would have a herd of cattle of my own.
- Q. Now, Mr. Vaught, was there any other source from which you could build up a herd of cattle other than the increase from the herd which the Vaughans turned over to you?
- A. No. I might qualify that by saying that there would have been another source, I could have purchased cattle providing I put this iron on them, the Vaughan iron on them, to help build up the herd, but I didn't have the financing to do it with so for that reason there was no other one.
- Q. What animals do you have to add into a herd of cattle in order to increase the size of it?
- A. Normally to build up your mother herd it is the heifers that you add into your herd."
- (R. 281)
- "Q. When did you first realize or ascertain that those heifer sales would have to be made?
- A. The final conclusion as to what heifers would have to be sold was after the cattle were rounded up and we determined what the income would be off of the steers and culled cows.
- Q. That decision was made at what time?
- A. During the fall of the year.
- Q. Was this sale of heifers during the term of this contract in the fall of each year, was that in keeping with your policy of herd management to which you testified concerning building up the herd?
- A. My intentions were to hold back every female I could in order to build it as long as I could during the life of the contract.
- Q. Why didn't you do that?

A. Because my obligations had to be met and the only source of money to meet those was through the sale of heifers.

Q. And those circumstances were foreseeable in advance?

A. No."

(R. 292)

Redirect Examination:

"Q. Mr. Vaught, you have told us about the mounting expenses of raising this herd and how this affected this problem of what animals were to be sold each year to raise the money to finance it. Did the price of cattle from year to year during this period increase commensurate with the increase of operating cost?

A. No.

Q. And if it had been the same proportion increase of cattle prices, why, then would you have been able to operate on the sale of steers and cull cows if the price of cattle had gone up to the proportion to the increase of operation?

A. I think very closely to it, yes, very few heifers we would have needed to have sold.

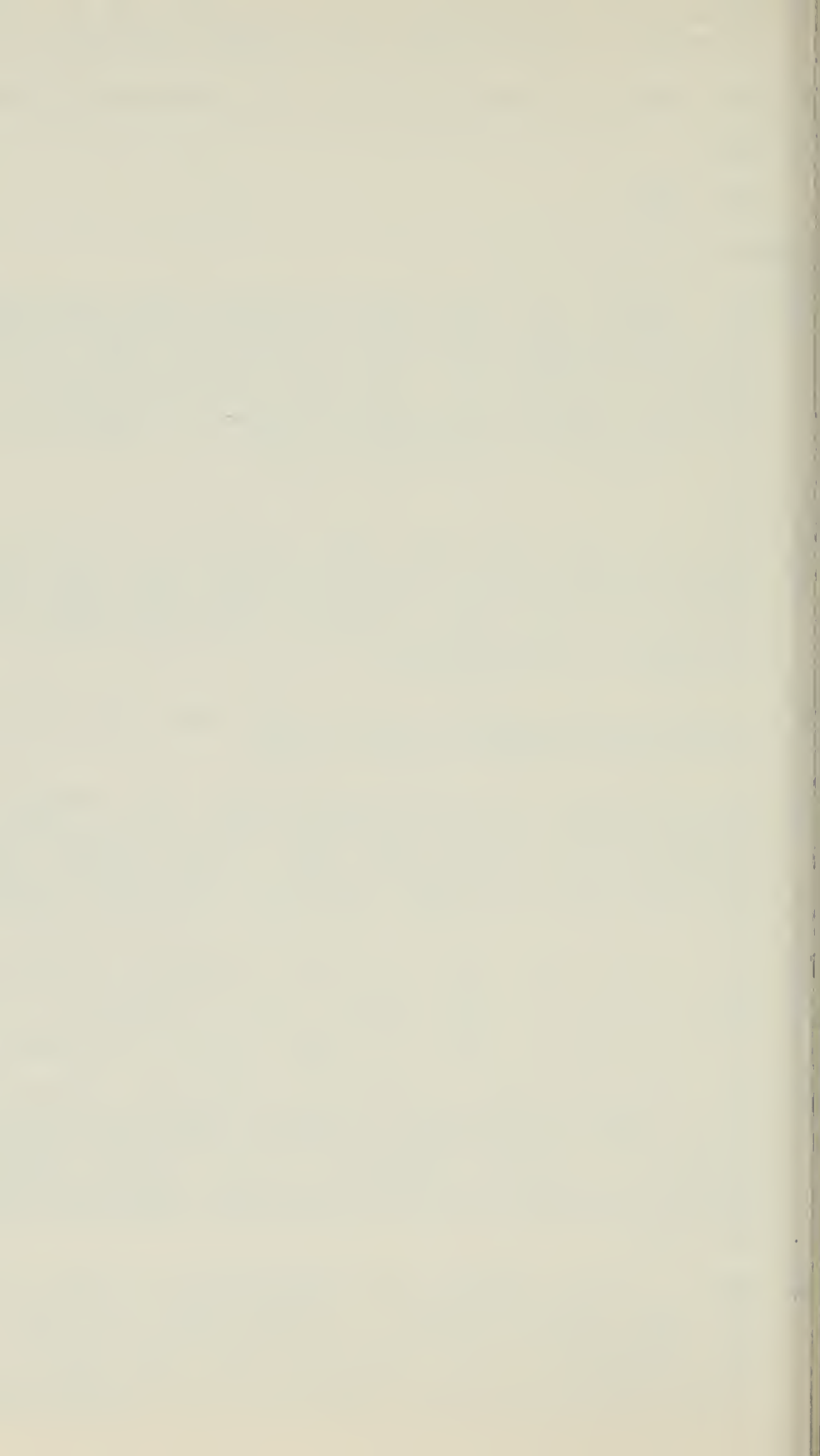
Q. You testified on cross-examination, Mr. Vaught, in the normal cattle range operation that it is customary to regularly sell each year some of the heifer crop. Would you say this operation of yours under the Vaughan-Vaught agreement was a normal operation in that regard?

A. No, I would say that it isn't a normal operation.

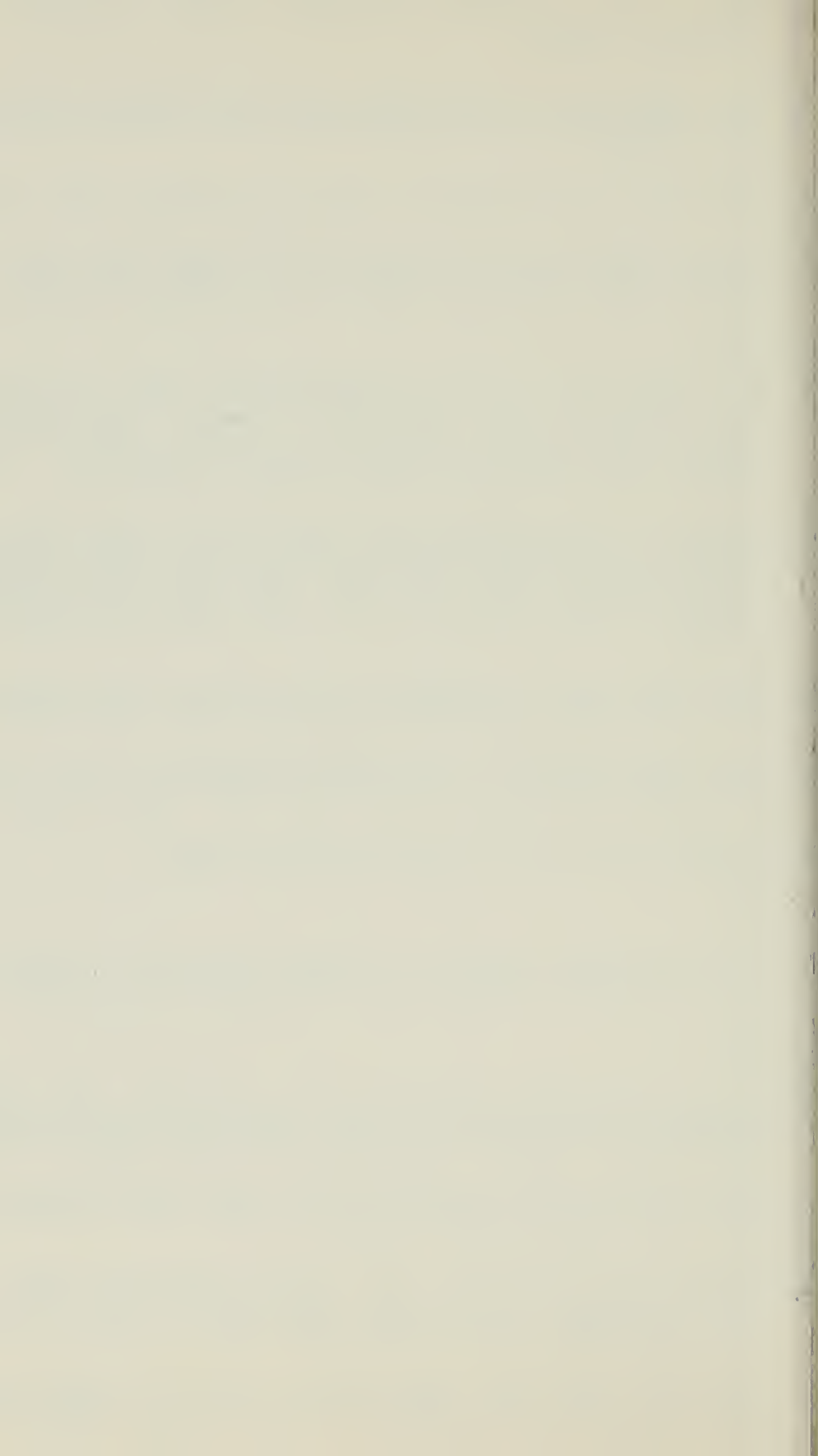
Q. What regard--in what manner was it abnormal as compared to the manner a herd of range cattle is normally operated?

A. Our intention was to increase our herd and build it up to a larger herd where a normal operation, you would think of a normal operation as one being stocked to capacity or near capacity, and the normal operation would be the culling out of old cows and replacing them with heifers.

Q. Well, if you had had the opportunity to have carried out your basic purpose of increasing the herd, then, as compared to the total animals turned over to you at the beginning of the contract what percentage of increase would you have expected it to accomplish?



- A. When I went into the contract I would increase it by a thousand head.
- Q. As compared to the number of head turned over to you at the beginning, what percentage of increase would that have been?
- A. Thinking right quick I would say 85 per cent increase.
- Q. This mounting cost of operation, was that the basic reason why you were unable to accomplish this?
- A. Yes.
- Q. You testified on cross-examination that you knew you were going to sell heifers, I think. When did you know, for example, in the fall of 1947 when did you first know you were going to sell heifers?
- A. After we had gathered the cattle and separated out the steers, determined about what their weight would be, their price, also the cows, that was the determining factor of the heifers to be sold and the number to be sold.
- Q. Did you know in advance of the sale in the fall of each of these years you were going to sell heifers?
- A. You would know as the season advanced in the late summer, it would be logical you would sell some of the heifers.
- Q. Would you know in the preceding year?
- A. No.
- Q. So were these sales of heifers planned in advance, that is, a year in advance or two years in advance?
- A. No.
- Q. As far as these heifers were concerned, when they were dropped what was your basic intention with respect to the future use of the animals in the herd?
- A. To use them as breeding cattle and leave them in the herd for replacement cattle.
- Q. Explain why that was your basic intention with respect to the female calves from the date of their birth, why was that your intention?
- A. That was the only opportunity I had to build the herd was through the retention of the female cattle."



Milford testified on cross-examination:

- "Q. You knew that you would only have one-half of the proceeds from the sale of the steers to operate on, is that correct?
- A. That is right. I knew that all of the proceeds for the steers I would have would be one-half, yes.
- Q. Was it not contemplated even as far back as the beginning of the period under the lease when you took over the operation that some of the heifers would have to be sold every year?
- A. I think I made this statement before, had I been able to operate as economically as Vaughan or as they told me they operated, and I have no reason to doubt the figures they gave me, had I been able to operate that economically with the size of herd of cattle that we had, we could have operated on one-half of the sale of the steers plus one-half of the sale of culled cows and retained all of the heifers."

(R. 361-362)

F. C. Vaughan testified with respect to the intent of the
partnership:

- "Q. At the time that Milford Vaught bought the T. Ranch and the related real estate, did you try to sell the cattle on that ranch to Milford Vaught?
- A. We offered them to him.
- Q. Did he buy them?
- A. No, sir.
- Q. Why not?
- A. He thought they were too high and he wasn't financially able to take them on.
- Q. Did he indicate to you at the time of the cattle agreement how he was going to operate the ranch?
- A. He indicated he was going to follow our pattern.
- Q. What pattern was that?
- A. They (sic) way we operate on the same selling basis, selling yearlings, and his intention was to build up that herd.

- Q. Do you know how Milford Vaught intended to stock that ranch?
- A. By raising the cattle off from the cattle of ours.
- Q. What was your intention with respect to the operation?
- A. We hoped he would do it.
- Q. Do what?
- A. Increase the herd. "

(R. 410-412)

APPENDIX "B"

Testimony of Vaughans and Milford Vaught with respect to selection of heifers for sale. Milford Vaught testified on direct examination:

- "Q. Will you explain the circumstances which controlled the decision concerning the number of cows and heifers to be sold each fall?
- A. I had certain obligations to meet, my only source of income was through the sale of cattle. I was operating on borrowed money and over the year I had borrowed so much money from the bank which had to be paid back and I had to sell enough cattle to meet those obligations. After the cattle were rounded up and the steers were classified, you had an idea about what the market was going to be and you had an idea about what the steers were going to weigh, you had so much income from that source and, in addition, you had so many culled cows to take up and when they were taken out and, you made the same determination as to about how many dollars they would bring, that was your next source of income. Then you had to either go to cutting into the cows or into the heifers for any additional income you felt you had to have to continue your operation.
- Q. Mr. Vaught, were these circumstances which controlled the decision concerning the sale of cows and heifers each fall, were those factors or circumstances foreseeable?
- A. No, not to a full degree. I might explain a little what I mean by that. When I went into the operation the Vaughans informed me they were operating for about a

thousand dollars a month, which would be twelve or maybe fourteen thousand dollars a year that it was costing them. When I got into the operation I found that I couldn't operate that economically for several reasons, one very important reason was there were two Vaughan brothers, one could be out with the cattle, the other could be with the ranch, he could supervise the ranching end of it and so on, the other one could be out supervising the cattle. With just myself then I found it was necessary to employ a good man, a reliable man to put out with the cattle which, of course, cost me additional money. My method of operating was considerably different than the Vaughans in some respects. The Vaughans operated, you might say, in my opinion, on a slipshod basis. If a piece of fence fell over they propped it up and that was good enough for now. If a head gate washed out, why, they drove some boards into the creek and that was good enough for now. I had never operated on that basis and to me that was home. As far as I knew from there on that was going to be home, so when I tried to fix up anything I tried to fix it up on a permanent basis and when I went out and fixed up a piece of fence I put in new posts and those things all cost me additional money to what it had cost the Vaughans."

(R. 289-91)

* * *

"Q. Now, what percentage again by years of these heifers that were sold each fall were with calf at the time they were sold?

A. I wouldn't know.

Q. Well, would you say that any of them were?

A. Yes.

Q. What percentage would you say were?

A. The only way that I could make any estimate of that would be part of the heifers that we retained for replacement heifers that weren't sold we figured in the neighborhood of a forty to fifty per cent calf crop from those two-year old heifers, that would be the only way that I could determine. Now, then, if at the time that we are classifying the cattle and selling them, if we could determine that one might be with calf, we don't sell that one, we hold it back for replacement heifer unless it was something of inferior quality we would want to let go."

(R. 308-9)



* * *

"Q. Yes. Will you explain, Mr. Vaught, how the gathering of the cattle process occurred?

A. When we were ready to start the roundup, the fall round-up--let me go back a little bit. We had what we called the calf roundup, after we turned the cattle out in the middle of March, and so on, then in June we rounded up the cattle and branded all of the calves that we could find. We speak of it as the calf roundup. Then in the fall after we had got the hay put up, and so on, and were ready to gather the cattle to sell what we intended to sell, we spoke of that as the beef roundup. When we got ready to stage the beef roundup we always advised the Vaughans we were ready for the beef roundup and one or both of them came over and assisted with the roundup, and the way we make these roundups, you ride a certain area and gather the cattle and take out the cattle that you want to take into the field. Now, you take in more cattle than what you are going to sell to get them classified into groups where you can cut out the ones that you don't want to sell and the ones that you do want to sell. Now, we wouldn't take every dry cow that was out there. Here is a good cow, she shows she is good age and maybe going to have a calf, and so on, but we gather far more cows than what we intended to sell. We would gather practically all of the heifers and we would gather all of the steers. We would gather all of the cows we could find with unbranded calves and in the Battle Creek operation we had 4,000 acres under fence, we would take those in the field, brand the calves, turn those back out and segregate the cows by placing the cows in one field, the steers in one field, and that would give us our determination about what the steers were going to weigh and how many we had gathered, and so on. Then we would work the cows and cut out the ones that we didn't want to sell and the ones we did want to sell, the ones that we wanted to sell we would keep in the field, the others would be turned back outside again. Then we would cut back the heifers, cut back the better heifers, the outstanding heifers we wanted to keep for replacement heifers and boil them down to what we figured we would have to sell to bring in the amount of money that was necessary for our operation."

(R. 325-6)

* * *

Cross-Examination of Milford Vaught:

"Q. You mentioned you had an operation on Lost River before you came up here into the Bruneau Valley?

Q. In your operations on the Lost River did you sell some of the heifers each year or did you keep them all?

A. No, we sold heifers, too.

Q. Is that customary to do that in the livestock operations of the type under the lease agreement you had?

A. It is customary to sell a certain amount of heifers.

Q. Could you tell us what would be a reasonable estimate of the percent you would normally sell?

A. Let me try to explain it this way.

Q. Take your time.

A. A normal operation where a person is stocked to capacity, each year you have a certain amount of old cows or cows that become defective for some reason or another that you cull out of the herd and you save replacement heifers to take care of them and I think in a normal operation where a man is stocked to capacity that probably it is in the neighborhood of ten to fifteen per cent of the heifers. It depends on his death loss and so on. If he has a heavy death loss it might be necessary to hold back 20 per cent of the heifers, but with an operation where you are trying to build up your herd and increase your herd and so on, then your desire is to hold all of the heifers that you possibly can so they will become mother cows and start producing for you.

Q. In the operation under the lease agreement, you would discover that you would have to sell heifers in any event, is that correct?

A. That I had to sell heifers what?

Q. In any event sell heifers each year.

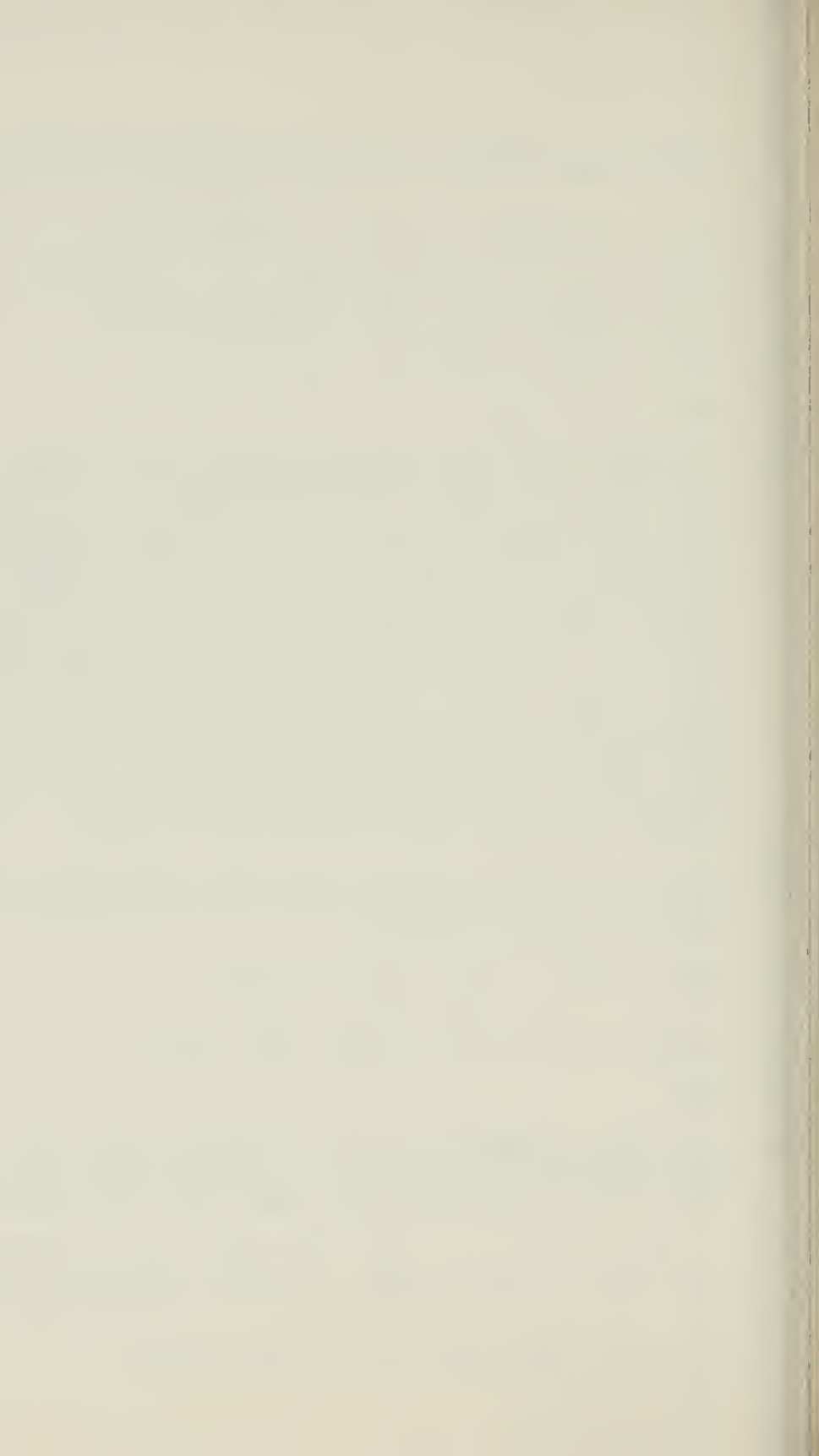
A. Yes.

Q. Did Floyd Vaughan or F. C. Vaughan ever tell you they had operated on the sale of steers alone in the operation they had before you came into the picture?

A. I don't know as if they ever made that remark. They did give me an estimate of their operating cost.

Q. Now, you knew you were going to receive but half of the proceeds from the sale of the steers?

A. That is right.



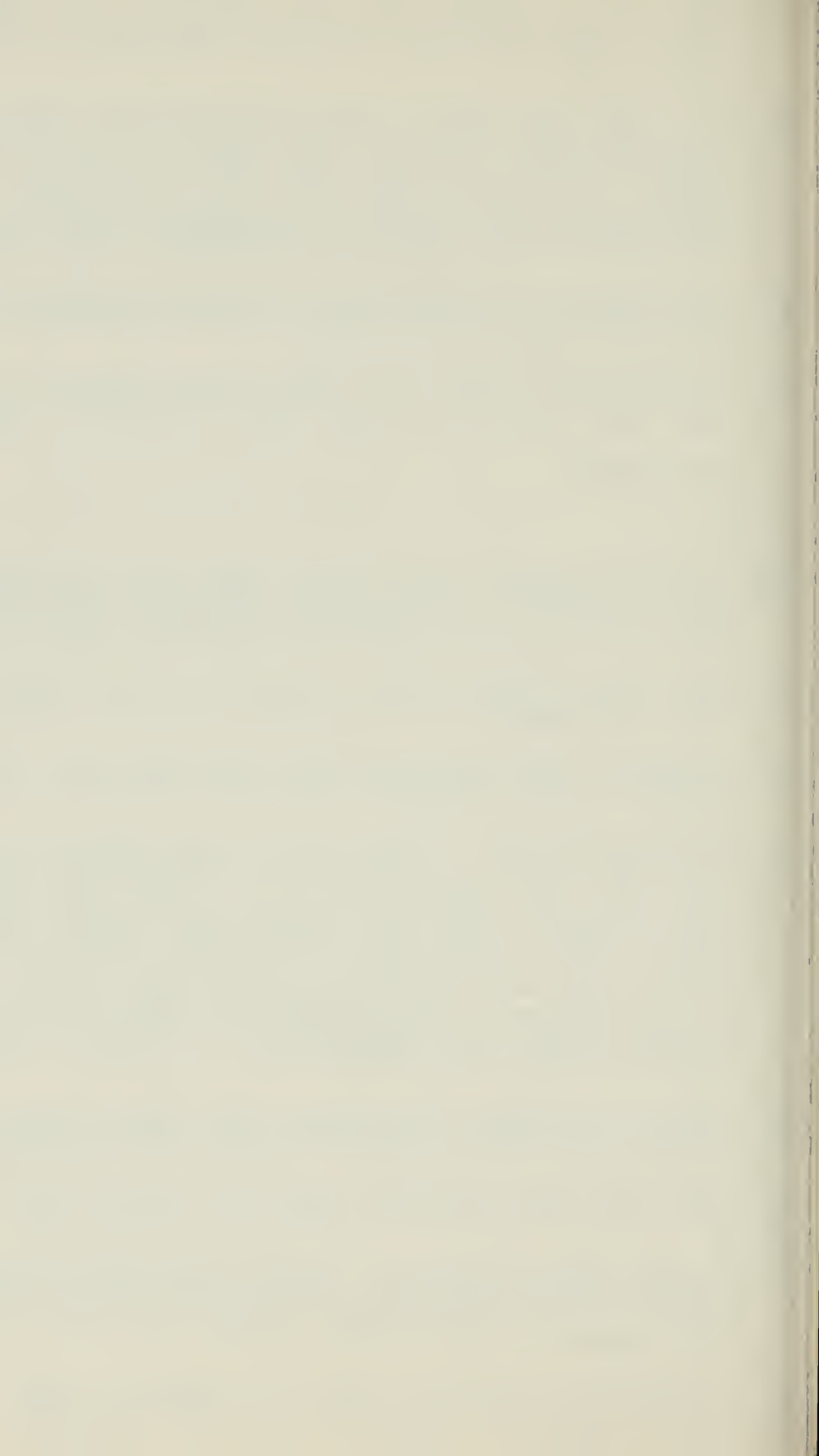
- Q. From this operation. From your experience would that lead you to believe that the proceeds from the steer sales alone would not cover the expenses of the operation?
- A. If I had been able to hold my operating costs as low as Vaughans held theirs or the figure they gave me, and I have no reason to doubt they were giving me a correct figure, if I would have been able to hold my operating costs that low I could have operated on the sale of one-half of the steers and one-half of the culled cows.
- Q. How long did it take until it became apparent that you could not operate that way?

A. I realized in the first fall we were going to have to sell some heifers or some cows in order to come out."

(R. 334-5)

* * *

- Q. In selecting the heifers for sale you have mentioned that you did have a certain method or certain process. You are trying to select the inferior ones, is that it?
- A. Yes, the better heifers are the ones you like to save for replacement.
- Q. As far as the inferior ones, you would have sold them anyway, would you not?
- A. Not necessarily. I am still in the process of building up a herd now and from our fall calf crop, last fall, that were baby beef last fall, I sold the steer end out of them, I kept all the heifers, didn't sell any of them. Now, as time goes on we may take the inferior heifers and sell them but we kept the entire group, but in the process of replacement of cattle you pick the better heifers for replacement. I think a successful operator always does that.
- Q. During the years in question the lack of operating funds on your part necessitated the sale of even good heifers?
- A. There were good heifers sold, yes, good cows sold.
- Q. By allowing heifers to run with the herd and be exposed to the bulls, generally, which was done on this operation, in your experience did this qualify for admission as a member of the breeder herd?
- A. I think it qualifies them as a member of the breeding herd. There are operators that are situated so they



can have fenced fields so they can take those heifers out and keep them separate, particularly the ones that they intend to sell. We weren't so situated so they became part of the breeding herd and we furnished bulls for them.

Q. But until the heifers started producing calves, you couldn't really determine she was a member of the herd, could you?

A. You mean of the breeding herd? She has been in with the breeding herd and been exposed to the bulls.

Q. That is about as far as you can say about these heifers until they reach a certain age and what age would you say, about two years old?

A. Well, you can go to determining on the heifer whether she is pregnant before time for her to calve, quite a ways, much farther in advance than you could with an older cow, but in making our selections in the fall of the year, if anything showed that they were calfy, of course, they went into the breeding herd. They might not have been as good quality as some heifers we sold, the price is not as good on one, the feeder doesn't want to put her in the feed yards. Anything that did show they were calfy were held in the breeding herd."

(R. 356-8)

* * *

Redirect Examination of Milford Vaught:

"Q. You testified on cross-examination, Mr. Vaught, in the normal cattle range operation that it is customary to regularly sell each year some of the heifer crop. Would you say this operation of yours under the Vaughan-Vaught agreement was a normal operation in that regard?

A. No, I would say that it isn't a normal operation.

Q. What regard--in what manner was it abnormal as compared to the manner a herd of range cattle is normally operated?

A. Our intention was to increase our herd and build it up to a larger herd where a normal operation, you would think of a normal operation as one being stocked to capacity or near capacity, and the normal operation would be the culling out of old cows and replacing them with heifers.

Q. Well, if you had had the opportunity to have carried out your basic purpose of increasing the herd, then, as

compared to the total animals turned over to you at the beginning of the contract what percentage of increase would you have expected it to accomplish?

A. When I went into the contract I would increase it by a thousand head.

Q. As compared to the number of head turned over to you at the beginning, what percentage of increase would that have been?

A. Thinking right quick I would say 85 per cent increase.

Q. This mounting cost of operation, was that the basic reason why you were unable to accomplish this?

A. Yes.

Q. You testified on cross-examination that you knew you were going to sell heifers, I think. When did you know, for example, in the fall of 1947 when did you first know you were going to sell heifers?

A. After we had gathered the cattle and separated out the steers, determined about what their weight would be, their price, also the cows, that was the determining factor of the heifers to be sold and the number to be sold.

Q. Did you know in advance of the sale in the fall of each of these years you were going to sell heifers?

A. You would know as the season advanced in the late summer, it would be logical you would sell some of the heifers.

Q. Would you know in the preceding year?

A. No.

Q. So were these sales of heifers planned in advance, that is, a year in advance or two years in advance?

A. No.

Q. As far as these heifers were concerned, when they were dropped what was your basic intention with respect to the future use of the animals in the herd?

A. To use them as breeding cattle and leave them in the herd for replacement cattle.

Q. Explain why that was your basic intention with respect to the female calves from the date of their birth, why was that your intention?

A. That was the only opportunity I had to build the herd was through the retention of the female cattle."

(R. 368-70)

* * *

Recross-Examination of Milford Vaught:

"Q. You were referring to the herd in some of your testimony. You mean the breeding herd when you were referring to the herd?

A. Referring to the entire herd?

Q. Yes. So when you were talking of heifers being part of the herd you don't necessarily consider them as being part of the breeding herd?

A. I considered them as being part of the breeding herd.

Q. You mentioned that steers were part of the herd. You didn't consider them to be part of the breeding herd?

A. No."

(R. 376-77)

. . . Vaughan testified that he helped gather the cattle for sale and every year of the contract (R. 350). With respect to the method of selection for sale or otherwise he testified:

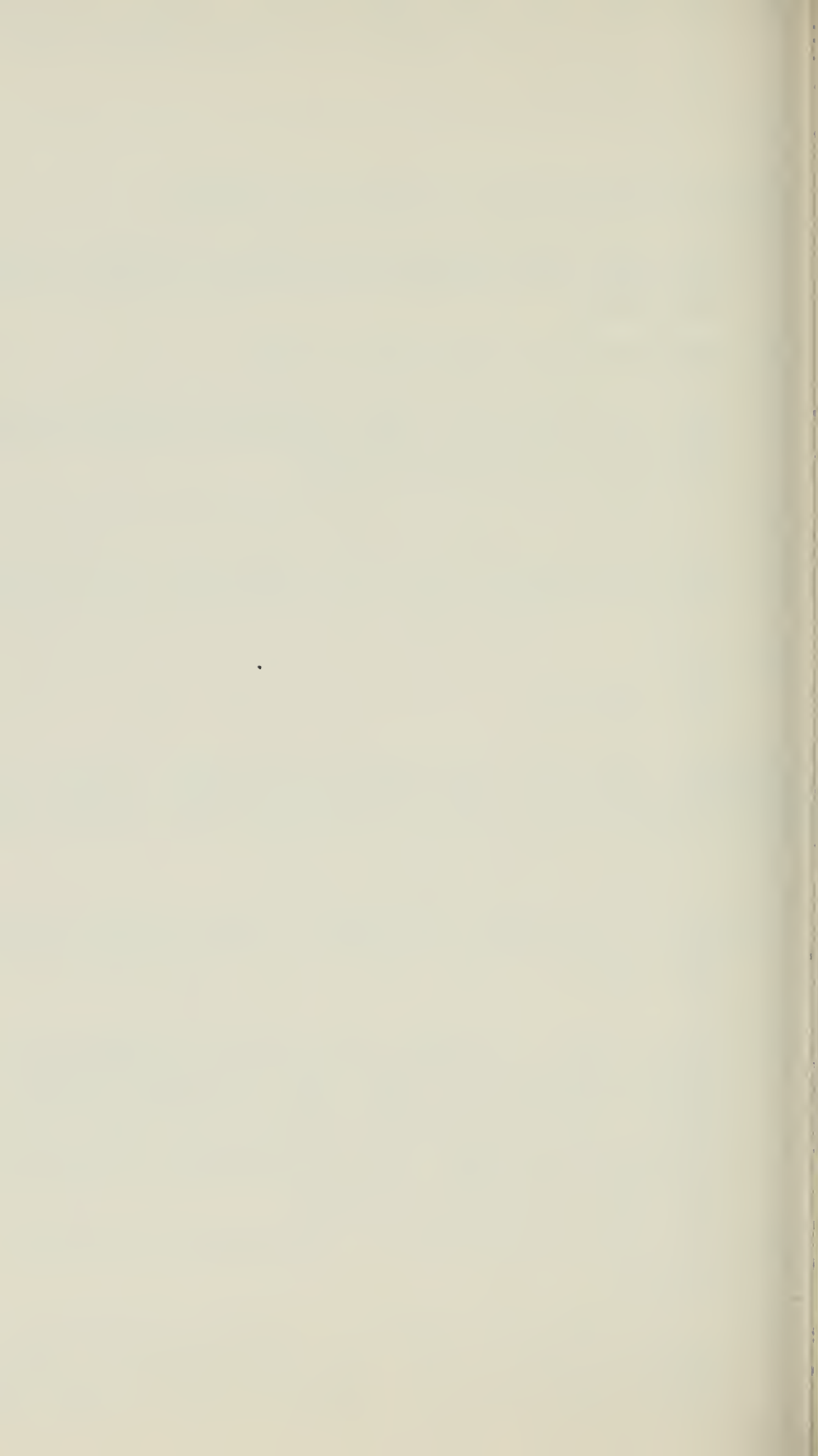
F. C. Vaughan Direct Examination:

"Q. Even though you intended to keep every animal that was fit for breeding, would it be necessary to sell off any cows?

A. Yes, there is always cows that are what we call breaking down, that is, getting old, and also spoiled bag cows and short milking cows and short breeding cows, that won't have a calf more than once in two years, you cull that stuff out of your herd annually if you have something to take its place. If a man hasn't he has to go out and buy some to take its place.

Q. How can you identify a cow that has no calf for two years?

A. A man knows his cattle; a cowman knows his cows just about as well as the city man knows his children. He knows each cow, in a sense, he don't know her name particularly, but he knows her and he observes if that



cow hasn't calved for maybe a year and isn't carrying on and he says, we will sell that cow this fall.

Q. What do you mean by calfy?

A. What do I mean by what?

Q. Calfy.

A. When she is showing calf.

Q. Even though you intended to keep every animal fit for breeding, would good husbandry require the sale of any heifers?

A. There would always be some culling in the heifers.

Q. For what reasons?

A. You got the long faced one, long necked one and off colored ones you don't want in your herd.

Q. At what ages do these--

A. (Interrupting) You can't do much of a job culling heifers until they are up in the yearling class.

Q. What age would that be?

A. Oh, fifteen to twenty-three months old."

(R. 411-12)

* * *

"Q. How would you determine how many heifers were to be sold?

A. I will tell you the way that was determined. Milford Vaught knew in a general way about how many steers he had and we would ride the range until he got those steers as close as he thought he could get them and he usually would have them within a five to ten per cent and in gathering the steers we would gather these cows as we came to them, an old cow and this kind of a cow. When we wanted them we would take them into the Battle Creek fields with the steers and we would gather some heifers along as we went through the gathering process, cut out the steers and cut out the cows and Milford would figure how much I am going to get and he would say, I got to have more money, so the next class of cattle he would have to go into would be the heifers, he would work up a set of heifers.

- Q. On what basis would you cull the heifers?
- A. On what basis cull the heifers?
- Q. What basis did you select the heifers on to be sold?
- A. We would select the heifers, the most undesirable ones to sell and we would keep the better ones. Now, I went over those figures here on this operation. During the four years under contest here, Milford's records show he sold 434 cows and lost and butchered 181. That makes a total of 613 head of cattle that he had to hold for replacement to keep the base herd and his numbers, it took 615 of these heifers during that span of years to replace the sold and lost. Now, if he had increased this herd a hundred head per year, he would have to have another head of heifers, if he increased this he would have to retain another hundred head of these sold heifers and then he would only have a five hundred increase at the end of these five years and that is the lowest number he ever anticipated having. Now, in this length of time there were 1,301 steers sold, so if you take the number of heifers sold and number of heifers it took for replacement, you see what he would have had to done, he would have had to kept them all but the culls."

(R. 415-16)

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- "Q. During that period of time what percentage of the heifers had calved at the age of twenty-four to twenty-six months?
- A. What per cent of the heifers would calve and did calve annually? Oh, I think maybe we got fifty or sixty per cent crop on the yearling heifers coming two year olds.
- Q. Based on that experience would it be a fair statement at least 60 per cent of the long yearlings sold, that they were pregnant?
- A. Only in this respect, in cutting these heifers, the people that was buying them didn't want the calviest heifers and we didn't want to sell them, so the calviest heifers were retained and we wanted to make the buyer believe all the rest were of calf, but it proved that they were."

(R. 425)

the testimony of the Vaughans and Milford was corroborated by
Marshall Anderson, a fully qualified cattle expert. He stated

"Q. You stated that most range operations ordinarily sold heifers in the ordinary course of their business. Now, where a range operation is operating less than the capacity of the ranch is that an economical operation?

A. To operate less than capacity?

Q. Less than capacity.

A. No.

Q. If they were operating at less than capacity and were building the herd would they still have certain heifers to sell?

A. They might have a few.

Q. What type heifers would they be?

A. Oh, they would be the heifers that would lack confirmation and probably drafting, hairless, there might be a small per cent, two or three.

Q. So there would always be culled heifers to sell from any range operation?

A. There would be."

(R. 399-400)

* * *

"Q. Now, in your experience as a cattle buyer of heifers, what percentage of heifers that you have purchased out of these range herds have you found to be pregnant either upon slaughter of those animals or upon placing those animals in a feed lot?

A. Usually 40 to 50 per cent.

Q. Did I understand you to say you had helped cull or rather helped cut out heifers at the Vaughan-Vaught operation?

A. Yes.

Q. When they were cutting out those animals from the main herd, on what basis would the heifers be selected to be sold?

A. Well, I wouldn't take the real calfy heifer. First, we would leave them on the Vaughan rack and then--I don't

know why they agreed to sell the heifers--I tried to take the straight barrel heifers, what we called straight barrels. I don't know why they sold them. I selected them because they were fleshy and everything. Those with more flesh were more desirable.

Q. You did not want the so-called calfy heifers?

A. That is right."

(R. 388-89)

